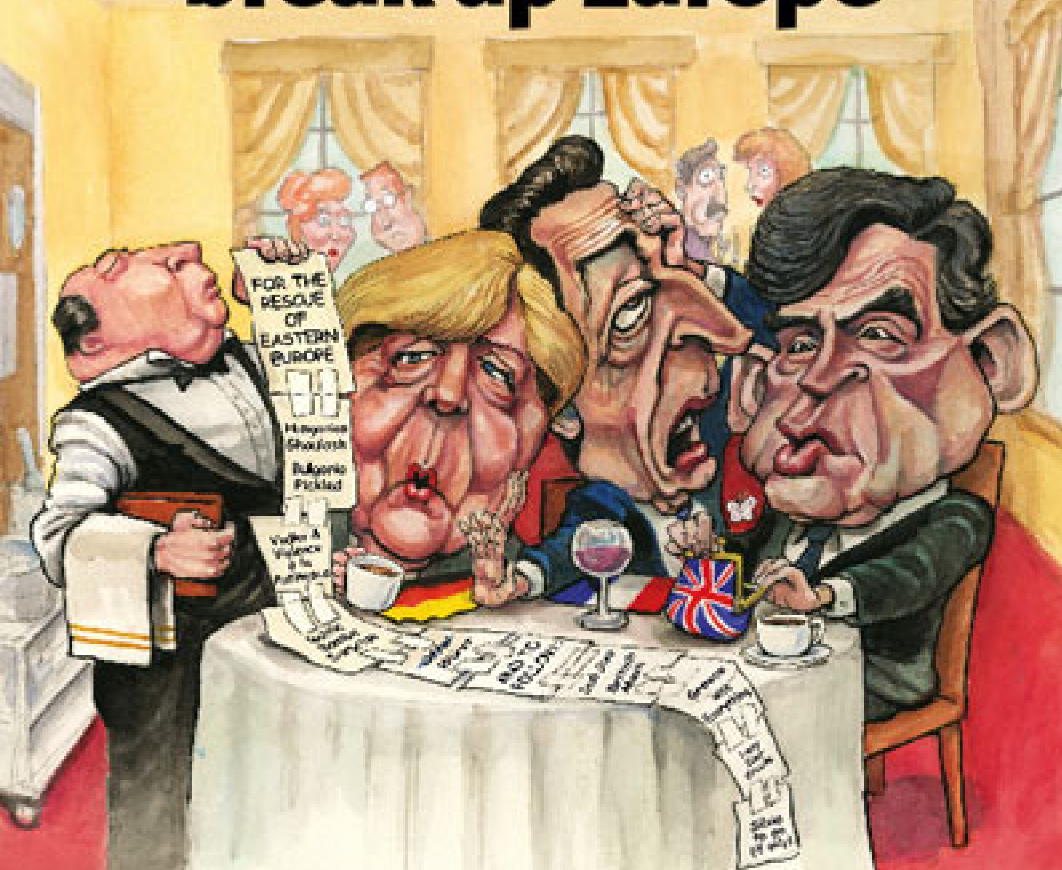
CLEANING UP: A 14-PAGE SPECIAL REPORT ON THE WASTE BUSINESS

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The bill that could break up Europe



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If eastern Europe goes down, it may take the European Union with it: leader



Europe

Britain

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International

Books & Arts

Obituary

Economic and Financial Indicators

Politics this week

Feb 26th 2009
From The Economist print edition

AP



Barack Obama made his first speech to Congress as America's president. Possibly taking note of criticisms that he has tended to sound apocalyptic about the economy, Mr Obama used the occasion to set out his administration's recovery plan, and stressed that he believed America would be stronger than before, to huge applause. His speech included an unwavering commitment to begin the process of reforming America's health-care system this year. See article

Mr Obama also prepared to send an outline of his **budget** to Congress, which proposed tax increases on the wealthy to pay for health care. The Democrats unveiled a $410 billion additional spending plan that they said was necessary to keep the government ticking over until the end of the fiscal year in September. See article

Mr Obama nominated Gary Locke as **commerce secretary**. Mr Locke, a Democratic former governor of Washington state and America's first Chinese-American governor, is the third candidate that the president has put forward for the job.

This land isn't your land

Despite the formation of a power-sharing government in **Zimbabwe** in which the prime minister, Morgan Tsvangirai, has promised to reimpose the rule of law, President Robert Mugabe's party accelerated the wave of confiscations of the few hundred remaining white-owned farms.

A new **South African** party, the Congress of the People, picked a Methodist bishop, Mvume Dandala, as its presidential candidate. Parliament chooses the head of state after a general election in April. See article

A special UN-backed court in **Sierra Leone** convicted the three most senior surviving commanders of the rebel Revolutionary United Front of crimes against humanity during the country's decade-long civil war.

The leader of **Israel's** right-wing Likud party, Binyamin Netanyahu, who was given first chance to form a coalition government, said he still hoped to bring Tzipi Livni and her centrist Kadima party into his governing fold. So far she has rebuffed him because of his refusal to countenance the idea of a two-state solution for Israelis and Palestinians. See article

Iraq's parliament lifted the immunity of a Sunni member, Muhammad al-Daini, in order to facilitate his arrest on charges of orchestrating a string of sectarian murders, including a suicide-bombing in parliament, car bombings and mortar attacks.

Who's in charge?

The police chief in Ciudad Juárez, on **Mexico's** border with America, resigned after drugs gangs, who had murdered his deputy, threatened to kill one of his officers every 48 hours until he quit.

President Álvaro Uribe of **Colombia** insisted he was a victim, not the orchestrator, of alleged snooping on politicians, judges and journalists by agents of the domestic intelligence service. See article

Argentina expelled a **Catholic bishop**, Richard Williamson, who caused outrage worldwide by denying the extent of the Holocaust.

As Raúl Castro marked his first anniversary as **Cuba's** leader, America's House of Representatives passed a measure easing sanctions. It now goes to the Senate. Richard Lugar, a senior Republican senator, also urged a rethink of policy.

Madame secretary

America's secretary of state, Hillary Clinton, visited **China**, where she stressed the importance of co-operation on combating climate change and the economic crisis. She refrained from public condemnation of China's record on human rights or Tibet. But the State Department's human-rights report subsequently accused China of a worsening human-rights record in some areas, despite last year's Olympics.

Exiled Tibetans called for a boycott of celebrations of the **Tibetan new year**, in memory of those who died in unrest a year ago. Foreign tourists planning to visit Tibet were told that the region would be closed to foreigners until the end of March. See article

AP

Dozens died after a gun-battle in Dhaka, **Bangladesh's** capital, between the army and mutineers from the Bangladesh Rifles. The mutineers were incensed at alleged discrimination against the Rifles' soldiers. Despite an amnesty offer, the mutiny spread to other towns and tanks were mobilised in Dhaka. See article

A Taliban leader in Bajaur, a **tribal area of Pakistan**, announced a unilateral ceasefire in fighting with the Pakistani army. This followed an agreed truce in the district of Swat in the North-West Frontier Province.

Defying predictions of their imminent military defeat, Tamil Tiger rebels in **Sri Lanka** launched an attack on Colombo using two light aircraft, both of which were shot down. The army claimed to be advancing on the last Tiger-held town in the north. See article

Uzbekistan's president, Islam Karimov, confirmed that he has agreed to allow America to transport supplies through the country for its troops in Afghanistan. But he said only non-military goods would be allowed through.

Harry Nicolaides, an Australian jailed in **Thailand** for writing a novel that broke local *lèse-majesté* laws, was granted a royal pardon.

Dropping like a stone

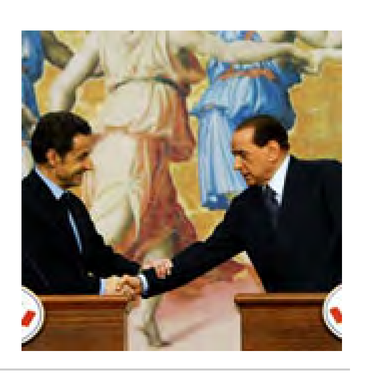
As worries grew about **eastern Europe's** economies and currencies, the Polish prime minister called a meeting of his fellow heads of government ahead of a scheduled European Union summit. Four east European central banks issued a co-ordinated statement suggesting that they may intervene to support their currencies. See article

Latvia's president began consultations to form a new government after the prime minister quit. Standard & Poor's, a rating agency, downgraded Latvian government bonds to junk status. **Ukraine's** debt was also downgraded, again.

A member of **Turkey's** parliament from a Kurdish party, Ahmet Turk, caused uproar by addressing the chamber in his native Kurdish. Turkish television immediately cut the live transmission of the debate as the Kurdish language is still banned in all state institutions.

AP

Italy and France signed a deal that is meant to pave the way for a revival of **nuclear power in Italy**. Silvio Berlusconi, the Italian prime minister, said he wanted to begin the construction of Italian nuclear-power plants.



Business this week

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America's Treasury released details about the **"stress tests"** that are being applied under the new **Capital Assistance Programme**. These gauge the capacity of banks with more than $100 billion in assets to weather a downturn under an adverse scenario in which unemployment rises above 10% next year and house prices fall by 27% over two years. Financial companies will have to raise more funds from the government if needed. The state may end up owning majority stakes in some banks. See article

Officials, however, played down talk of full bank **nationalisation**. Sheila Bair, the head of the Federal Deposit Insurance Corporation, said there was "ambiguity in the word". The Treasury readied a third rescue plan for Citigroup. See article

Amid the uncertainty, **stockmarkets** endured a difficult week, with the Dow Jones Industrial Average closing at its lowest level in nearly 12 years.

It's come to this

The British Treasury spelt out the details about its **Asset Protection Scheme**, in which a bank's riskiest assets will be "ring-fenced" and under which the government will cover up to 90% of future losses. **Royal Bank of Scotland** was the first to join, placing £302 billion ($430 billion) of assets in the scheme and taking a "first loss" of £19.5 billion. The bank, which is majority state-owned, reported a net loss of £24 billion for 2008, the biggest in British corporate history. See article

Northern Rock offered to provide £14 billion ($20 billion) in new mortgage loans. The announcement came a year after the bank was nationalised. The British government, which will help fund the loans, is taking further steps it hopes will boost lending.

JPMorgan Chase slashed its shareholder dividend from 38 cents a share to 5 cents. The news surprised investors. The bank maintained that its first-quarter performance so far is "solidly profitable" and capital is "strong". Its decision will save it $5 billion a year.

Denmark's financial authorities seized control of Fionia Bank. It is the third Danish bank to be nationalised since the autumn.

Picking up the pieces

After less than two years in the job, Marcel Rohner resigned as chief executive of **UBS** with immediate effect. The new boss of the troubled Swiss bank is Oswald Grübel, the former head of Credit Suisse. UBS has reported massive write-downs and the biggest-ever Swiss loss. It was recently forced to divulge the names of some clients to American tax authorities, igniting a row between American and Swiss banking regulators over Switzerland's secrecy rules.

China's **Hunan Valin Iron & Steel** took a 16.5% stake in **Fortescue Metals**, the third big investment by a Chinese firm in an Australian mining company in as many weeks.

Anglo American became the latest mining company to lay off employees because of falling commodity prices. The company will cut 19,000 jobs, 10% of its global workforce.

Japan's exports fell by 45.7% in the year to January. The country's exports to the United States dropped by 53%, to Europe by 47% and to China by 45%. Japan's car exports declined by 69%. Many Japanese manufacturers have already made swingeing job cuts as they adjust to the downturn.

General Motors reported a net loss of $9.6 billion for the last three months of 2008, and $30.9 billion for the whole year. Its liquidity position worsened in the quarter. Meanwhile, **Saab**, GM's Swedish unit, which it has put up for sale, filed for bankruptcy protection after Sweden's government refused a bail-out.



Vattenfall, a Swedish electricity provider, agreed to pay €8.5 billion ($10.8 billion) for the non-grid business of **Nuon**, a Dutch counterpart. The deal will eventually create Europe's biggest operator of offshore-wind energy; both companies are big in renewable and clean energy, including solar and tidal power.

Hearst, a media conglomerate, warned that it would sell or close the *San Francisco Chronicle* "within weeks" if savings from cost-cutting measures, including a significant reduction in staff, did not succeed. The West Coast's second-biggest newspaper has seen losses mount since the dotcom bubble burst in 2000-01.

Leaving the family

Peter Chernin, one of Hollywood's most prominent executives, quit as president and chief operating officer of **News Corp**. He will also step down as boss of the Fox group of film studios and television stations, which will now report direct to Rupert Murdoch. Mr Chernin was at the Fox Searchlight party at the Oscars this week to celebrate the success of its film "Slumdog Millionaire", which won best picture. See article

KAL's cartoon

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Illustration by KAL



The bill that could break up Europe

Feb 26th 2009
From The Economist print edition

If eastern Europe goes down, it may take the European Union with it

Illustration by KAL



TUMBLING exchange rates, gaping current-account deficits, fearsome foreign-currency borrowings and nasty recessions: these sound like the ingredients of a distant third-world-debt crisis from the 1980s and 1990s. Yet in Europe the mess has been cooked up closer to home, in east European countries, many of them now members of the European Union. One consequence is that older EU countries will find themselves footing the bill for clearing it up.

Many west Europeans, faced with severe recession at home, will see this as outrageously unfair. The east Europeans have been on a binge fuelled by foreign investment, the desire for western living standards and the hope that most would soon be able to adopt Europe's single currency, the euro. Critics argue, with some justice, that some east European countries were ill-prepared for EU membership; that they have botched or sidestepped reforms; and that they have wasted their borrowed billions on construction and consumption booms. Surely they should pay the price for their own folly?

Yet if a country such as Hungary or one of the Baltic three went under, west Europeans would be among the first to suffer (see article). Banks from Austria, Italy and Sweden, which have invested and lent heavily in eastern Europe, would see catastrophic losses if the value of their assets shrivelled. The strain of default, combined with atavistic protectionist instincts coming to the fore all over Europe, could easily unravel the EU's proudest achievement, its single market.

Indeed, collapse in the east would quickly raise questions about the future of the EU itself. It would destabilise the euro—for some euro members, such as Ireland and Greece, are not in much better shape than eastern Europe. And it would spell doom for any chance of further enlarging the EU, raising new doubts about the future prospects of the western Balkans, Turkey and several countries from the former Soviet Union.

The political consequences of letting eastern Europe go could be graver still. One of Europe's greatest feats in the past 20 years was peacefully to reunify the continent after the end of the Soviet empire. Russia is itself in serious economic trouble, but its leaders remain keen to exploit any chance to reassert their influence in the region. Moreover, if the people of eastern Europe felt they had been cut adrift by western Europe, they could fall for populists or nationalists of a kind who have come to power far too often in Europe's history.

How to avert disaster

The question for western Europe's leaders is how best to avert such a disaster. Although markets often treat eastern Europe as one economic unit, every country in the region is different. Three broad groups stand out. The first includes countries that are a long way from joining the EU, such as Ukraine. Here European institutions may help financially or with advice, but the main burden should fall on the International Monetary Fund. These countries will have to take the IMF medicine of debt restructuring and fiscal tightening that was meted out so often in previous emerging-market crises.

Things are different for the countries farther west, all EU members for which the union must take prime responsibility. One much-touted remedy is to accelerate their path to the euro, or even let them adopt it immediately. It might make sense for the four countries with exchange rates pegged to the euro: the Baltic trio of Estonia, Latvia and Lithuania, plus Bulgaria. (Slovenia and Slovakia have joined the euro already.) None of these will meet the Maastricht treaty's criteria for euro entry any time soon. But they are tiny (the Baltics have a population of barely 7m), so letting them adopt the euro ought not to set an unwelcome precedent for others nor should it damage confidence in the single currency. Yet the European Central Bank and the European Commission firmly oppose this form of "euroisation", even though two Balkan countries, Montenegro and Kosovo, use the euro already.

Unilateral or accelerated adoption of the euro would make far less sense for a third group of bigger countries with floating exchange rates: the Czech Republic, Hungary, Poland and Romania. None of these is ready for the tough discipline of a single currency that rules out any future devaluation. Their premature entry could fatally weaken the euro. But as their currencies slide, the big vulnerability for the Poles, Hungarians and Romanians, especially, arises from the debt taken on by firms and households in foreign currency, mainly from foreign-owned banks. What once seemed a canny convergence play now looks like a barmy risk, for both the borrowers and the banks, chiefly Italian and Austrian, that lent to them.

Stopping the rot

The first priority for these four must be to stop further currency collapse. The second is to prop up the banks responsible for the foreign-currency loans that are going bad. The pain of this should be shared four ways: between the banks and their debtors, and between governments of both lending and borrowing countries. From outside, these two tasks will necessitate help from several sources: the European Central Bank as well as the IMF, the commission's structural funds, the European Bank for Reconstruction and Development and perhaps the European Investment Bank. Given the scale of the problem, the lack of co-ordination between these outfits has been scandalous. A third aim must be to get eastern European countries to restart the structural reforms they have evaded thus far.

Bailing out the same mythical Polish plumbers who just stole everybody's jobs will be hard for Europe's leaders to sell on the doorsteps of Berlin, Bradford and Bordeaux, especially with the xenophobic right in full cry. German taxpayers are already worried that others are after their hard-earned cash (see article). The bill will indeed be huge, but in truth western Europe cannot afford not to pay it. The meltdown of any EU country in the region, let alone the break-up of the euro or the single market, would be catastrophic for all of Europe; and on this issue there is little prospect of much help from America, China or elsewhere. It is certainly not too late to rescue the east; but politicians need to start making the case for it now.

The White House and America's banks

In knots over nationalisation

Feb 26th 2009
From The Economist print edition

State control of some banks is sadly unavoidable. Don't run away from it; focus on doing it well

AP



THERE is a whiff of Alice in Wonderland about the arguments over America's banks. Voices on the free-market right, including Alan Greenspan, a former chairman of the Federal Reserve, and a clutch of Republican senators, suggest that temporary nationalisation may be best for the most troubled big banks. Rather than drip-feeding public support, they argue, the state should take over those banks that have all but failed, clean up their balance sheets and then quickly sell them.

Meanwhile the Democratic Obama administration considers nationalisation taboo. The White House's plans involve injecting more public funds into the biggest banks if new "stress tests" suggest they need it (see article). Addressing Congress on February 24th, Mr Obama made clear that taxpayers would probably have to find more cash. But nobody will admit that this could lead to public control, let alone explain how control would work. This week both Tim Geithner, the treasury secretary, and Ben Bernanke, the Fed chairman, publicly dismissed nationalisation, saying it was not necessary.

Oh dear! I shall be too late

Unfortunately, that is a false hope. A strategy geared to avoiding outright government control will not work as well as one that is honest about what it wants to achieve and how. Nationalisation should not be a goal of policy, but the worsening economy, the scale of likely bank losses and the banks' lack of capital means that some will survive only with a capital infusion big enough to leave them largely in public hands.

Look at Citigroup, which has already been propped up by $45 billion of non-voting government capital and guarantees to limit losses on some $300 billion of its worst assets. As *The Economist* went to press, Citi was on the brink of converting part of the Treasury's aid into a government equity stake as high as 40%. If more capital is needed (as most expect), the Treasury will probably have either to embark on Enron-style creative accounting, or to become a majority shareholder.

Although the administration is unwilling to admit this, the speculation outside government has been that nationalisation is only a matter of time. That has fed a devastating uncertainty. In the past week bank stocks have swooned on fears that shareholders in troubled banks will eventually be wiped out. Led by collapsing bank shares, the Dow Jones Industrial Average fell to an 11-year low on February 23rd. Although bank shares recovered slightly after Mr Bernanke's comments, that says more about shareholders' relief at the stay of execution than about a sudden improvement in the banks' prospects.

The uncertainty over nationalisation is costly and self-defeating. Several big banks have seen their borrowing costs rise as bondholders fear that they, too, will suffer in any government restructuring. Weaker share prices and dearer credit will worsen the economy, further weaken banks' loan books and increase the need for yet more public capital.

It is time for America to move beyond sloganeering and denial. Contrary to the glibness with which some proponents advocate it, government control of big banks is not a quick and painless solution to the banking mess. Given the scale of the crisis, the depth of the recession and the burden of the underlying debt, government involvement in any bank is unlikely to be unwound quickly. Sweden, widely praised for its handling of its early 1990s banking bust, took several years to clean up and privatise the banks it nationalised. Mr Obama's people are right to worry about the risk of bureaucratic management and political meddling in lending decisions.

You are old, Father Ben

Yet politicians, including Mr Obama's team, are already meddling. Congress has imposed sweeping controls on bankers' pay; banks that receive public capital must already provide regular reports on how much they lend and to whom; complaints from within Citi suggest that managers are distracted and bewildered by demands from politicians and regulators about day-to-day operations. Mr Obama this week left little doubt that he wants more oversight.

Explicit government ownership would be an improvement over the onerous, fiddly and capricious intervention of today. An arms-length bank management board would both keep the interferers at bay, and also require the public sector to bear the consequences of its meddling on the bank's performance. Rather than an escalation of public control, as government capital is gradually converted into common equity to cover the banks' losses, it would be better to lay out the scale and scope of public ownership as soon as possible.

The administration's "stress tests" may show that some banks need a lot of capital. If the government has to provide it, taking control as it does so in some cases, so be it. If the government becomes the owner, it needs to act as such, selling businesses, breaking them up and firing managers if needs be.

If that happens, shareholders will be heavily diluted—though, crucially, they will not be wiped out, as investors now fear. It is tempting to suggest that the bondholders of big banks should suffer too, just as they can suffer when small banks fail and are taken over by the Federal Deposit Insurance Corporation. Though that would indeed set an example (and drastically lower the cost to the public purse) it risks a catastrophic Lehman-style flight from all bank debt. With their noses held, the Obama team should state plainly and clearly (as the Swedish did) that these banks' liabilities will be left whole.

The odd thing is that Mr Obama's fiscal policy has been far clearer. The budget, due to be presented on February 26th, promises to eschew accounting gimmicks, paint an unvarnished picture of America's fiscal future, and to reduce the deficit to 3% of GDP by 2013. It is not perfect—there is too little focus on entitlement or tax reform (see article). But it seems an honest attempt to put the recent stimulus in the context of a plausibly responsible medium-term fiscal path. Laying out the template of bank rescues is harder, but no less important. Unless America's financial system recovers, the economy will remain in a funk and Mr Obama's budget goals will turn out to be as elusive as the world beyond the looking glass.

Investor relations

To forecast or not to forecast?

Feb 26th 2009
From The Economist print edition

Beware firms that refuse to issue annual financial targets

Illustration by Claudio Munoz



DIVINING what the future holds is tricky at the best of times; at the worst, it is devilishly difficult. So why bother? Citing the chaos of the global downturn, a growing number of companies, including Unilever, an Anglo-Dutch consumer-goods firm, Costco, a big American retailer, and Union Pacific, one of America's big railroads, have decided not to give annual earnings estimates for 2009.

If ever there was a moment for firms to keep their crystal balls under wraps, this may appear to be it. But many companies are still issuing annual forecasts in spite of the uncertainty roiling their markets. On February 24th, for instance, Home Depot, another American retailer, estimated that its revenues and earnings per share from continuing operations would decline by about 9% and 7% respectively in its 2009 financial year. Earlier this month, Reckitt Benckiser, another European consumer-goods group that competes with Unilever, said it was confident it could increase its revenues by 4% this year.

Issuing such targets is pointless and dangerous, critics claim. They argue that, with the banking industry catatonic and consumers pulling their purse strings ever tighter, the world is so topsy-turvy that any financial goal will be out of date as soon as the ink dries on the press release. Moreover, when companies then issue a *mea culpa* and lower their forecasts, disappointed investors will hammer the price of their shares. To avoid this punishment, managers will be tempted into short-termism, slashing investment in research and development or new machinery, for instance, even if that damages their firms' longer-term prospects. Better, then, to stay mum rather than risk a mauling.

But such arguments do not mean that companies should ditch forecasts altogether. Precisely because peering into the future is harder today than it was a year ago, managers should be using every available means to gauge what the world could look like in the coming months and to establish targets using this analysis (see article). And they should draw up contingency plans for cutting costs without damaging vital investments if revenues fall short. Indeed, firms that shy away from forecasting should attract extra scrutiny from shareholders. It may indicate that managers are underprepared, or that they are trying to use the turmoil as an excuse to avoid setting goals for which they could be held accountable.

Target practice

What about the charge that firms issuing annual forecasts could be punished if they miss them through no fault of their own? This has a lot to do with the sort of numbers firms give. Managers ought to think twice before issuing a single, headline number for most financial targets. Even when things were rosy,

such spuriously accurate figures were of less use than a description of how the main factors affecting a business could change. Given the dire state of the global economy, such information should now often be accompanied by a range of potential outcomes for the most important financial indicators.

Some firms could be tempted to issue ranges that are so wide you could drive a double-decker bus through them. But if they do, then investors will rightly conclude their chief executives do not have a tight grip on the business. It will take some effort to convince everyone that a range of outcomes makes more sense—analysts love to punch headline numbers into their spreadsheets. So here is one forecast for 2009 that is certain to come true: investor-relations departments will be busier than ever.

China and Tibet

Another year of the Iron Fist

Feb 26th 2009
From The Economist print edition

If this is success, maybe China should look for an alternative

AFP



AS TIBETANS around the world this week marked the advent of the new year of the Earth Ox, many did so in a spirit of mourning rather than jubilation. The festival fell just before a bloodstained anniversary season: 50 years since the Chinese suppression of an uprising that saw the Dalai Lama, their spiritual leader, flee into exile in India with some 100,000 followers; 20 years since protests that led to the imposition of martial law in the capital, Lhasa; one year since ugly and murderous anti-Chinese riots in Lhasa that brought a sharp and lasting security backlash. The fact that so many troops are still needed, merely to prevent commemorative protests, suggests that China's Tibet policy is in need of an overhaul.

China's officials seem to be contemplating nothing of the sort. Indeed, they may believe things are going their way. A year ago Tibet seemed a real threat to China's hopes of presenting the Beijing Olympics as an unblemished celebration of its achievements. As the Olympic torch was carried round the world, it was met from London to Delhi by protests against Chinese rule in Tibet. Yet the Olympics themselves passed with no serious protest or international boycott.

Since then Tibet has slipped down the international agenda. In her first overseas visit as secretary of state, Hillary Clinton recently stopped in Beijing to beseech China's co-operation in fixing the world economy and stopping the planet from frying. In the apparent belief that China, oddly, will not pursue such aims out of its own self-interest, she forbore from harping on issues such as human rights and Tibet.

Chinese diplomats, meanwhile, are cock-a-hoop at a concession they wrung last October from Britain, whose government had hitherto been the only one not formally to recognise China's "sovereignty" in Tibet, accepting instead only its "suzerainty" (ie, de facto control) over the region. Apparently unaware of the importance of the issue to both China and exiled Tibetans, Britain changed policy in a bland and obscure statement published on the internet. At talks with the Dalai Lama's representatives in Beijing the following week, China, perhaps not coincidentally, hardened its position even further. The talks, in which China has never appeared sincere in offering any compromise to the exiles, now seem more futile than ever.

Himalayan clouds

Yet the refusal to talk to the Dalai Lama comes at a cost. This week, in both what China misleadingly calls the "Tibet Autonomous Region" and in adjoining provinces, security has been intense (see article). Foreigners have been kept out. Tibet has been closed. China can easily quash any protests by those foolhardy enough to mount them. But repression is hardly the way a successful, modern power wants to

govern.

In 1959 the Dalai Lama's escape from his homeland produced a myth: that he had conjured up a belt of cloud to hide his retinue from the Chinese air force. At the time, *The Economist* scoffed at this (see article). "The real cloud", we argued, "was evidently the unity of the Tibetan people in their hatred of Chinese military rule." Sadly, despite all the economic advances, despite the easing of Chinese policy after the Cultural Revolution, and despite (indeed, because of) the influx of Han Chinese into Tibet, that assessment remains largely true today. Sadly, too, the Chinese explanation for unrest remains unchanged: in 1959, as now, it was blamed on a "few reactionaries manipulated by foreign powers".

The chief reactionary, of course, is the Dalai Lama himself, whom China still vilifies. It seems to believe that its Tibet problem will be solved with his passing. In fact, it is more likely to worsen. The Dalai Lama, unlike many of his followers both in Tibet and in a remarkably cohesive exiled population, accepts Chinese rule. He demands merely that "autonomy" should have substance. And for all China's accusations against him, he has never wavered in his insistence that his followers pursue their aims peacefully. China may one day come to regret spurning his moderating influence.

The waste industry

A load of rubbish

Feb 26th 2009
From The Economist print edition

What's wrong with policies on waste, and how to get them right

Corbis



AT POPE'S CREEK, on America's Potomac river, there's a pre-Columbian rubbish tip of oyster shells covering 30 acres, to an average depth of ten feet. Humanity has always produced waste in vast quantities; but more people, more consumption and the contribution emissions from rubbish make to climate change mean that disposing of the stuff is an increasingly contentious issue.

People feel that they have a natural right to throw away as much stuff as they like, just as those lucky native Americans chucked the shells from their plentiful oyster piles over their shoulders. They shouldn't. Rubbish damages the environment and is expensive to dispose of. With household waste, just as with toxic chemicals, governments need to persuade people that they should be responsible for the muck they produce.

Trashy regulations

Americans are the champions of trash: on average they jettison over 700kg each a year. But developing nations are catching up fast. By 2030, Indians will be producing twice as much as they are now; Chinese people three times as much.

Waste is also becoming more hazardous. Modern industry produces many things, from coal ash to computers, that are difficult to dispose of properly. The consequences can be grotesque: in the city of Dzerzhinsk, in Russia, decades of slapdash handling of chemical waste has reduced male life expectancy to just 42 years. Rotting waste, meanwhile, produces methane, one of the more potent greenhouse gases, and thus contributes to global warming.

Yet as the special report on the waste business in this week's issue argues, there are grounds for optimism amid the mounds of rubbish. Environmental concerns have spurred dramatic improvements in the way waste is managed in many countries. Recycling is becoming ever more common. Entrepreneurs are brimming with schemes to turn rubbish into electricity or fuel or fertiliser. Environmentalists dream of a world in which almost nothing is wasted.

But it is governments that have the power to turn such visions into reality, and their policies are all over the place. In America, for example, landfills containing household rubbish are subject to stringent regulation, whereas ones filled with toxic sludge from power plants are less tightly controlled. In Britain landfills are taxed out of all proportion to the damage they do the environment. In poor countries many governments often ignore waste altogether. Only 6% of Madagascar's rubbish is even collected.

To clear up the mess, governments need to hold people and companies responsible for the waste they produce. One way of doing that is to work out the cost of disposal and charge firms and households for rubbish collection based on the volume they produce. That helps discourage people from chucking stuff out, and provides a revenue stream to dispose of it when they do. Another is to oblige manufacturers to take back and dispose of certain goods when consumers have finished with them. That gives firms an incentive to make their wares easy to recycle or re-use.

As consumers, people hate paying for rubbish disposal. But as voters, they claim to worry about the state of the planet. Such measures are the price of cleaning it up.



On Abraham Lincoln, Argentina, Rio Tinto, savings, the stimulus package, subprime lending, environmentalism

Feb 26th 2009
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An alternative history lesson

SIR – Lexington's column on "the war over Lincoln" mentioned the vast number of books that have been written about the civil-war president (February 14th). Few of these works, however, fully recognise the South's political triumph, only a decade after Appomattox, that reversed the Union's military victory. In the disputed presidential election of 1876 several southern states gave their support to the Republican candidate, Rutherford Hayes, in return for the withdrawal of the remaining federal troops, who had been protecting blacks. Southern whites quickly restored, in all but name, their "peculiar institution" of slavery, and reinforced their dominance by lynching some 3,400 blacks over the next half-century.

Lincoln's pyrrhic victory stands in striking contrast to the record of other 19th-century emancipators, who achieved better results through peaceful means. In Russia Alexander II ordered the emancipation of the serfs in 1861. In Brazil the liberal Dom Pedro II came to power in 1840 and all of Brazil's slaves were freed long before he died as an exile in Paris in 1891.

It wasn't until Lyndon Johnson's administration that Lincoln's intentions were achieved. Johnson himself predicted that the passage of his civil-rights legislation would result in the demise of the Democratic South. Meanwhile, the party of Abraham Lincoln morphed into the party of Jefferson Davis.

William Burke
San Francisco

SIR – Lincoln's main priority was to preserve the Union not to abolish slavery. Indeed, the Great Emancipator famously remarked that "if I could save the Union without freeing any slave I would do it." On hearing of Lincoln's death Edwin Stanton, the secretary of war, uttered "now he belongs to the ages." Perhaps it is best we just leave it at that.

Andy Dolan
Palm Desert, California

Argentina's monetary policy

SIR – Your article on the economies of Argentina and Uruguay stated that Argentina has pursued an expansionary monetary policy ("Profiting from virtue", February 7th). This is incorrect. To better understand our approach one must recognise that Argentina has had a long history of macroeconomic instability and fiscal and external imbalances, which led to periods of high inflation and a highly dollarised economy.

In our emerging economy the private credit market remains highly segmented and is equivalent to only 12% of GDP, compared with an average of 30% for Latin America, weakening the power of monetary policy to affect aggregate demand. Argentina's economy is still cash-intensive, so the power of fiscal and wage policies to affect demand and expectations is predominant. Therefore, it is critical to track the recent evolution of fiscal and wage policy together with monetary aspects when making judgments about expansionary policies.

Furthermore, to help weather the international financial crisis we are building buffers, such as accumulating foreign reserves, and making sure our financial system is solvent and highly liquid. The Central Bank is committed to pursuing a robust monetary policy through the strict control of the growth of the means of payment.

Monetary aggregates have been growing at diminishing rates since 2004. In fact, private sector M2 is growing at less than 10%, far below the growth of nominal GDP. This is consistent with the monetary programme presented every year before Congress and which aims to maintain the equilibrium between supply and demand in the monetary market. Preventing a new crisis is a priority: it is imperative that we pursue a dual mandate of monetary and fiscal stability.

Martín Redrado
Governor Central Bank of Argentina
Buenos Aires

Wrong on a rights offering

SIR – When reporting on Rio Tinto's proposed investment deal with Chinalco, you stated that "alternative methods of financing, notably a rights offering, would have certainly been dilutive" ("Undermined", February 14th). I've noticed that Rio's chairman, Paul Skinner, also thinks this, which is astonishing. The whole point about a rights issue is that it does not dilute existing shareholders and that the discount at which it is done is irrelevant in financial terms, though it may have some relevance in terms of sentiment, etc.

Peter Townshend
Cape Town

Home truths

SIR – Buttonwood's "lament for savers" was spot-on (February 14th). The entire thrust of the economic bail-out is centred on keeping people in their homes, rewarding those who behaved in a financially irresponsible manner. I must not be a Keynesian as I do not believe that saving money and acting prudently puts people out of work. If I save money it does not go under the mattress, it goes into a bank or other financial institution and thereby makes its way into the stream of commerce. If I forgo an expensive latte at Starbucks, the marginal cost is lost to Starbucks. It is not lost to the overall economy if the money is instead deposited in a bank. In times past, this money would have been recorded in my account and loaned out to responsible borrowers and my savings would have had a multiplier effect.

Michael Brautigam
Cincinnati, Ohio

Balancing taxes

SIR – You suggested that Republicans fear a "'tax tipping-point', when a majority of Americans pay little or no taxes and discover that they can vote themselves goodies paid for by others" ("Gloom offensive", February 14th). As if to prove it you go on to say that "the top 20% of earners pay 69% of federal taxes, and that share is rising".

Republicans may well be perturbed that uneven tax burdens erode democratic values, but they should have concerned themselves long ago with the unbalanced distribution of income. Census Bureau data shows that in 2007 the top 20% of households received half of America's total household income. The mean household income of "the top 20%" was 14.5 times that of the bottom 20%.

William Clay
Charlotte, North Carolina

SIR – Sadly, the Republicans have rediscovered the joys of opposition. Nothing as slight as a national crisis is going to make them shift from ground that seems so politically advantageous. Yet despite its considerable flaws, the stimulus bill does have substantial broad support—among voters. Perhaps, in time, the Republican rump will come around, but I would not count on it any time soon, especially when newspapers such as yours are prepared to treat their claims of high-mindedness with such undeserved respect.

John Moukad

Cambridge, Massachusetts

SIR – What we need is a system that allows citizens to have their say on expenditures before they become law. In a format similar to that used by the television show “American Idol”, I’d like to see senators being given five minutes to make a case for their earmarks and pet projects before a panel of three adjudicators, who will review and question their statements. The proposals can then be presented to the American people for an up-or-down vote.

Joe Rosen
Lincoln, Massachusetts

The following letters appear online only

The causes of the financial disaster

SIR – Your leader on the future of finance remarkably failed to address the root cause of the financial crisis: subprime lending in the United States (“Inside the banks”, January 24th). “Greed”, which has been with us since the expulsion from the Garden of Eden, and “overpaid investment bankers” did not suddenly spawn millions of loans to people with bad credit and few prospects of paying the money back. Government did that.

The United States’ government as a matter of policy pressured banks to make subprime loans or lose their ability to expand and grow. First by law, and then by regulation, Fannie Mae and Freddie Mac were systematically forced to increase their purchase of subprime loans to 56% of their holdings.

The fundamental thesis of your article is that mathematical models failed. Whether that is so or not is beside the point. The dice did not come up snake eyes three times in a row by chance, they were loaded. The United States’ government, by politicising mortgage lending in America, tainted the quality of the securitised mortgages that were injected into the arteries of the world’s financial system. Although an expansive monetary policy and the massive inflow of cheap money helped inflate the housing bubble, the financial crisis as we know it would not have occurred without the toxic effect of subprime lending.

Even with greed, highly paid aggressive bankers, credit-default swaps, and those geeky quants, we would almost certainly have muddled through the fallout from the bursting of the housing bubble without a full-blown financial crisis had there not been millions of mortgages made to people with chequered credit and no down-payments. Securitised subprime mortgages destroyed the asset base of banks, and with it, the trust and confidence upon which the financial system depends.

Regulators in the United States had total power over subprime lending but as the bubble built, they used that power not to raise down-payments or credit standards, but to lower them. The problem was not that regulators were not empowered, the problem was that they were not alarmed. Worse yet, they used their power to promote a political agenda that spawned the crisis in the first place.

You lament that “regulation...often owes more to politics than it does to sound finance” (A special report on the future of finance, January 24th). Walter Bagehot knew it could never be otherwise. While we should try to improve mortgage standards and deal with the specific problems that the crisis has brought to light, the wholesale regulation of the financial system, based on the false premise that the core of the system is flawed, would give us the worst of both worlds: no growth and no stability.

Phil Gramm
Former chairman of the Senate Banking Committee
Washington, DC

Nerds for nature

SIR – Your article on the battle over a power line in southern California banishes all of us who are concerned with nature conservation to one unthinking corner of the green tent (“Tree-huggers v nerds”, February 14th). In fact, groups like ours are keenly aware of economic and environmental trade-offs and of the need to save species cost-effectively. Furthermore, when we question a development project, the first test is whether it yields a positive net present value, in other words whether development value is

realised in return for environmental losses.

The world is littered with boondoggles that consume wealth rather than produce it and also do harm to the climate, biodiversity, or both, in the bargain. So, if you'll consider expanding your category of climate nerds to some few "nerds for nature", know that there are many of us out here that will be proud to have the title.

John Reid
President
Conservation Strategy Fund
Sebastopol, California

Ex-communist economies

The whiff of contagion

Feb 26th 2009
From The Economist print edition

Eastern Europe's woes are not unmanageable. But they are not being managed. The result could be catastrophe



AMID the wreckage of Latvia's retailing industry, which has declined 17% year on year according to the latest figures, one item is selling well: T-shirts with seemingly mysterious slogans such as "Nasing spesal". Latvians are glad to have something to laugh about, even if it is only their finance minister, Atis Slakteris. In an ill-judged foreign television interview, using heavily accented and idiosyncratic English worthy of the film character Borat, he described his country's economic problems as "nothing special".

Put mildly, that was an original interpretation. Fuelled by reckless bank lending, particularly in construction and consumer loans, Latvia had enjoyed a colossal boom, with double-digit economic growth and a current-account deficit that peaked at over 20% of GDP. Conventional wisdom would have suggested applying the brakes hard, by tightening the budget and curbing borrowing. But the country's rulers, a lightweight lot with close ties to business, rejected that. Fast economic growth made voters feel that European Union membership was at last producing practical benefits, after a disappointing start when tens of thousands of Latvians went abroad in search of work, leaving rural villages and small towns depopulated.

The central assumption, in Latvia and many other countries in or near the EU, was that convergence with rich Europe's living standards and other comforts was inevitable. Lending in foreign currency went from 60% of the total in 2004 to 90% in 2008. Why pay high interest rates in the local currency, the lat, when the cost of a euro loan was so much cheaper? In a few years Latvia would surely join the euro anyway. Similarly, worries about financing the inflows were dismissed: Swedish banks would no more abandon their subsidiaries in Latvia than they would pull out of, say, southern Sweden.

Last year tested those assumptions nearly to breaking point. First, Latvia's housing bubble popped. Then the main locally owned bank, Parex, went bust and had to be nationalised, amid fears that it could not pay two syndicated loans due this year. In December Latvia accepted a humiliating €7.5 billion ($9.56 billion) bail-out led by the IMF.

The big cuts in social spending that the package entailed led to vigorous public protests. Now the government has resigned. At a time when strong leadership and public trust are needed more than ever,

the country's squabbling and discredited politicians look hopelessly out of their depth. Latvia is an economic pipsqueak, with just 2.4m people. But the rest of the region is watching nervously, fearful that more bad news from the Baltics could bring others crashing down too.

It is easy to be pessimistic. This is indeed the worst economic crisis since the collapse of the communist planned economies and the wrenching process of privatisation, liberalisation and stabilisation that followed. The main ex-communist economies are likely to contract by 3% this year, according to Capital Economics, a consultancy. Yet the picture is not uniform. Only a few countries have needed an IMF bail-out. One is Latvia, whose economy is set to contract by at least 12% this year, and whose credit rating has just been downgraded by Standard & Poor's to junk. Another is Hungary, burdened with a larger debt-to-GDP ratio than almost any other new EU member. It received $25 billion in October and faces a contraction of up to 6%. A third is Ukraine—chaotically run, corrupt and badly hit by the slowdown in its main export market, Russia. Ukraine's IMF deal brought it $4.5 billion in November. But a second tranche of $1.9 billion is stuck; the deal is unravelling as politicians squabble over spending cuts. Its economy is likely to shrink by 10% this year. Other countries with IMF packages agreed or pending include Belarus (a Russian ally which is still expected to see growth this year), Georgia (which was bailed out after last year's war with Russia) and Serbia.

Most other countries in the region are faring much better, though. Poland—by far the largest economy of the new EU members—is nowhere near collapse. Unlike its central European neighbours, it is big enough not to depend chiefly on exports to the rest of the EU. By European standards, its public finances are in fairly good shape. Its debt-to-GDP ratio is below 50%. Growth will be negligible, or slightly negative, but nobody is forecasting a big decline. Some Polish firms and households have taken out foreign-currency loans—but the figure is around 30% of all private-sector lending, compared with twice that in Hungary.

The second-biggest economy, the Czech Republic, is in good shape too. Its economy may shrink by 2%, but it has a solid banking system and low debt. Its neighbour Slovakia is in better shape still: it managed to join the euro zone this year. Like Slovenia, which joined two years ago, Slovakia can enjoy the full protection of rich Europe's currency union, rather than just the indirect benefit of being due to join it some day.

Farther afield, the picture is very different. For the poorest ex-communist economies, the problem is not financial meltdown. They lack much to melt. Their exports are raw materials, agricultural products and people. In six countries, money sent home by foreign workers counts for more than 10% of GDP (in Tajikistan and Moldova it is more than 30%). Outsiders who agonise over the Latvian lat or Hungarian forint are rarely bothered with worries about the somoni (Tajikistan), leu (Moldova) or manat (Turkmenistan).

That highlights an important problem. Outsiders tend to lump "the ex-communist world" or "eastern Europe" together, as though a shared history of totalitarian captivity was the main determinant of economic fortune, two decades after the evil empire collapsed. Though many problems are shared, the differences between the ex-communist countries are often greater than those that distinguish them from the countries of "old Europe" (see table).

Fourteen ways to slowdown

In euro area
Pegged to euro

Country	GDP per person*	S&P credit rating†	Financing requirements % of GDP‡	Exports§	In a nutshell
Belarus	12,344	B+	7.3	62.1	Autocratic, isolated, gained surprise IMF bail-out
Bulgaria	12,372	A	29.4	61.0	Strong finances back currency peg, but sleaze rampant
Czech Rep.	25,757	AA	9.4	80.1	Thrifty and solid, but hit by export slowdown
Estonia	20,754	AA	20.0	72.0	Star reformer squeezes spending to stay afloat
Hungary	19,830	A	29.9	80.2	Currency crash could topple debt-heavy economy
Latvia	17,801	BBB	24.3	46.6	Clinging to currency peg amid turmoil and downturn
Lithuania	18,855	A+	27.1	59.0	Painful spending squeeze to avoid worse
Poland	17,560	A+	13.2	42.3	Regional heavyweight speeds up euro bid
Romania	12,698	BBB+	20.2	34.4	Spendthrift policies meet sober reality
Russia	16,161	BBB	2.2	31.7	Energy-based kleptocracy in denial about crisis
Serbia	10,911	BB-	23.5	22.2	Seeking more IMF help
Slovakia	22,242	AAA	12.5	90.5	Smugly in euro area but hit by car-factory slowdown
Slovenia	28,894	AAA	–	70.5	Self-satisfied, rich and still growing
Ukraine	7,634	CCC+	16.1	45.0	No end in sight to political and economic chaos

*PPP$, 2008 estimate †Standard & Poor's, latest ‡Current-account balance, principal due on public and private debts plus IMF debits, 2008 estimate §Goods and services, % of GDP, 2008 estimate

Sources: IMF; Moody's; Economist Intelligence Unit; *The Economist*

They range from distant, dirt-poor despotic places to countries in the EU that are not just richer than some of the old ones, but have better credit ratings, sounder public finances and stronger public institutions. In almost any contest for good government, stability or prosperity, Slovenia (under a sort of communism until 1991) looks better than Greece, which invented democracy and was never communist.

The thirst for capital

Historical and geographical quibbles aside, what the ex-communist countries have shared over the past decade is a mighty thirst for capital. Having missed out on decades of growth and integration with the outside world, almost all (a few oddballs in Central Asia aside) are trying to catch up. Money from abroad has come in from borrowing on the bond market, from foreign direct investment or from selling shares. Most often it has come through bank loans.

At one extreme is Russia, which enjoyed huge external surpluses thanks to its wealth of raw materials. But its big companies borrowed lavishly on the strength of that, creating a potential short-term debt problem. Russian corporate borrowers have to pay back around $100 billion this year. At the other extreme lie countries such as Slovakia. They attracted billions from foreign car manufacturers, drawn by a skilled workforce, low taxes and decent roads in the heart of high-cost Europe.

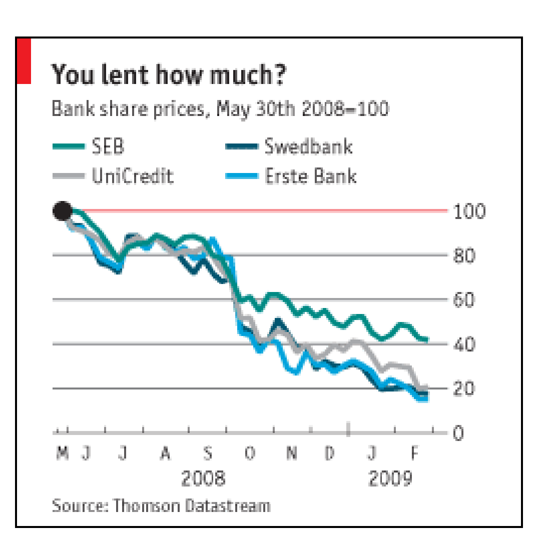
Countries that relied chiefly on foreign direct investment are the least vulnerable now. The new factories may shut down. But it is harder for that capital to flee. Those that rely on foreign investors buying their bonds, such as Hungary, are the most vulnerable: their fortunes vary with every twitch of a trader's fingers. In the middle are those that rely on lending from foreign banks to their local subsidiaries. That looked solid in the boom years, as Western banks scrambled to win market share by offering good terms to borrowers and lenders in the fastest-growing bit of Europe. It is still highly unlikely that any Western bank will pull the plug on a subsidiary anywhere—even in troubled Ukraine.

But nerves are jangling. The ex-communist countries have survived the first phase of the crisis, thanks to their own policies and some external support. The second phase, in which the rich world is turning stingier and possibly more protectionist and lenders are scurrying to safety, may be harder. The ex-communist economies must repay or roll over a whopping $400 billion-odd in short-term borrowings this year. Coupled with the lazy but easy lumping of nearly three dozen countries together, that creates the region's biggest danger: contagion (see article). In other words, failure in one place sparks a disaster in another, even though it may be far away and have the same problem in a far more manageable form.

Contagion could happen in many ways. One is if depositors lose confidence that their savings are safe. So far, Western-owned banks have enjoyed rock-solid credibility: more so, in many cases, than governments

or other public institutions. But that confidence could be undermined. If only one foreign bank pulls the rug from under one local subsidiary, leaving depositors stranded, it will cloud perceptions of banks' reliability across the region. The most dangerous kinds of bank runs would be those in which depositors try to pull out either their foreign currency, or local currency which they would then attempt to convert into hard currency. In some countries that could overwhelm the ability of the central bank to support the financial system.

Another weak point is where shareholders take fright. If a foreign bank with big exposure to the region—Swedish, Austrian or Italian—needs to raise more capital but finds that outsiders think its loan book is too risky, what happens? The price of rescue may be that it sheds a troubled foreign subsidiary. Signs of shareholder twitchiness are growing (see chart).



For now, the most likely source of contagion is collapsing currencies. The paradox is that for countries with floating exchange rates, an orderly depreciation would in normal circumstances be a good way of cushioning an external shock, such as the slump in export markets now hitting the ex-communist economies. It stokes competitiveness and, along with lower interest rates, it lays the foundations for a return to growth. Governments with sound public finances might also consider running a looser fiscal policy to counteract the downturn.

Propping up the currency

For most of the countries in the region, such a textbook response is out of the question. Some have currency boards, or pegged exchange rates. In the Baltic states these have been the centrepiece of economic policy for more than 15 years. Abandoning them would not only bankrupt big chunks of the economy that have borrowed in euros. It would also be a huge psychological blow to public confidence in the whole idea of independent statehood. These countries have suffered the most painful part of being in the euro zone—the inability to devalue and regain competitiveness—without getting all the benefits.

Countries with floating exchange rates have a bit more room for manoeuvre. Their problem (a big one in Hungary, a lesser one in Romania and Poland) is that falling exchange rates may bankrupt the firms and households which have, in past years, taken out unwise loans in foreign currencies, chiefly euros and Swiss francs. That was, in effect, a convergence play. If you believed your country was heading for the euro zone some time in the next few years, then why not take advantage of the low interest rates there, rather than suffer the higher ones in your domestic currency?

What seemed a minor risk back then now looks painfully mistaken. For those earning forints or Polish zloty, the big swings in exchange rates in recent weeks have sent the size of both loans and repayments spiralling upwards. The zloty has dropped 28% and the forint 22% against the euro since the middle of last year. If the East Asian crisis of 1997 is any guide, these and other currencies may yet have further to fall.

This risk of a currency collapse will limit these countries' options. So far many big central European countries have cut interest rates heavily to try to boost their economies—Poland's central bank cut its policy rate again this week. But currency weakness will limit their room for manoeuvre. The Czech, Hungarian and Polish central banks issued a co-ordinated statement this week hinting they might intervene to support their exchange rates. But that route is tricky. Russia has blown half its reserves in a series of unsuccessful attempts to try to prop up the rouble.

Spending and tax policies would be another way of dealing with a downturn. But these are constrained, too. Those countries with a chance of joining the euro are scrambling to cut their budget deficits to get them in line with the 3% of GDP target set by the EU's Maastricht treaty. Yet that aggravates the problem. The danger for Latvia and Ukraine is a downward spiral, where cuts in public spending damage the economy in a way that helps to entrench the deficit.

So far, the economic crisis has not translated into populist or protectionist politics. It is the east European countries that have been demanding that the rest of the EU stick by the rules of the single market. Their development over the past decades has been thanks to the free movement of capital, goods and labour. They would like a lot more of it: in a contest to subsidise industries, rich countries always win.

But that stance will not hold indefinitely if things get worse. Willem Buiter, a prominent economist, believes it is only a matter of time before some of the ex-communist countries introduce capital controls. That, in theory, would allow them to concentrate on stabilising their economies without worrying so much about the external value of their currency. If voters find the economic pain of adjustment unbearable, politicians can pass laws that will make foreign-currency borrowings repayable in local currency. That would be met with fury by the foreign banks, who would in effect see their loan books expropriated. But it could happen.

Against that background, what can be done? The east European countries are, belatedly, co-ordinating their approach within the EU, holding their own mini-summit on March 1st. They want to embarrass countries such as France for what they see as its protectionist approach to the crisis. They are supporting each other: the Czech Republic and Estonia were among those contributing to the Latvian bail-out.

But even co-ordinated local efforts are unlikely to make much difference, given the scale of the problem. The real lead, and the real money, must come from outside the region. That brings into play a slew of political problems. Having trumpeted their free-market principles in past years, and dismissed the stodgy approach of countries such as Germany and France, the new EU members from eastern Europe are now turning to old Europe in the hope that it can hurry up the flow of EU structural funds to counteract the downturn, bail out or prop up over-exposed banks in places like Austria, and stretch the rules of the European Central Bank to let it provide support to countries outside the euro zone. The case for such measures is strong, and it is in the interest of all Europe that contagion is contained. But that does not mean that it will happen.

Green shoots

Feb 26th 2009 | TALLINN
From The Economist print edition

Doom and gloom are not universal

EVEN allowing for snow, the medieval Old Town of Tallinn is unnaturally quiet. The best restaurant, Pegasus, has only one table occupied: your correspondent's. Shops are offering colossal discounts, even bigger than the painful spending and wage cuts passing through parliament in its pastel-painted palace on the hill above the city. But Endel Siff, a local businessman, is eager to talk about something else: drug-detection machines. Those made by his firm use advanced laser-fluorescence technology: more accurate, simpler, cheaper and more robust, he says, than the gas-chromatography apparatus in common use so far. Mr Siff's company, Nar Test, employs 60 people and is expanding fast.

Admittedly, Mr Siff is hardly typical. One of the richest men in Estonia, he has an uncanny sense of timing. He left the lucrative oil-transit business before it was hit by Russian sanctions in 2007. He baled out of his country's overinflated property market before that bubble burst. He even sold most of his shares.

But he highlights an important point, often lost amid the glum headlines. This is not 1989, when the then-communist states tiptoed back into a capitalist world that for many was bafflingly unfamiliar. The institutions built and the human and financial capital gained during the past 20 years will not disappear overnight. And this is not the 1930s, when the economic slump pushed every country bar the then Czechoslovakia into autocratic rule. That decade ended with Europe's most destructive war.

Ex-communist countries are more resilient and flexible than countries with happier histories. They have had to be, and it may stand them in good stead now. And though some bits of the economy (and in some countries most bits) may be doing dreadfully badly, the crisis is also a chance to hire newly available workers, find cheap premises and capture markets abandoned by others.

The government's finances

Brave rhetoric, grim reality

Feb 26th 2009 | WASHINGTON, DC
From The Economist print edition

The biggest threat to Barack Obama's good fiscal intentions is the economy

Getty Images



FOR a man who is likely to run a budget deficit in excess of 12% of GDP this year, Barack Obama can do a surprisingly good impression of a fiscal hawk. Just days after signing into law a huge $787 billion fiscal stimulus, he kicked off a "summit" of congressional leaders, administration officials and policy wonks by warning of "another crisis down the road as our interest payments rise, our obligations come due".

A day later, on the night of February 24th, he gave his first address to the joint houses of Congress. He declared that the "day of reckoning has arrived" and Americans must confront their "mountain of debt". But he also promised that no family earning less than $250,000 would have to pay "one single dime" more in taxes.

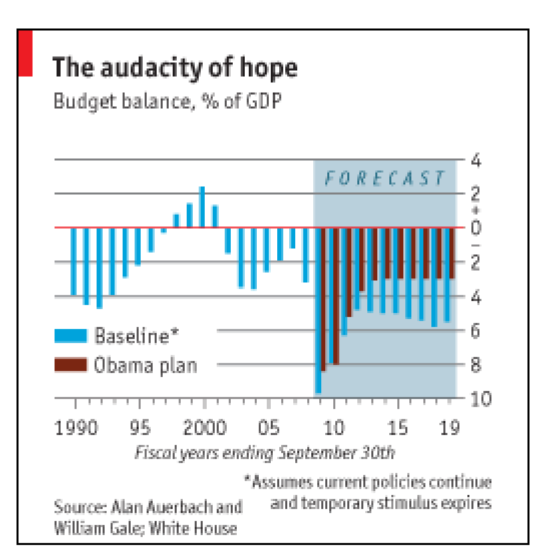
On February 26th, as *The Economist* went to press, the president was due to unveil a draft budget that promises to cut the deficit from a vast $1.75 trillion in fiscal 2009 (which ends this September) to $533 billion in 2013, when his first term ends. As a share of GDP, the draft has the deficit falling from this year's post-war high of 12% to just 3%.

Is that promise credible? At a minimum, Mr Obama seems more fiscally honest than George Bush, whose accounting gimmicks vied with Enron's. Mr Bush's budgets routinely excluded unavoidable outlays, such as those for wars and natural disasters, incorporated tax increases and spending trims that he knew would never occur, and masked his policies' impact on the deficit by shortening the forecast horizon to five years from ten. Mr Obama puts most of the missing items back in the budget, and restores its horizon to ten years.

To boost revenue, Mr Obama will let Mr Bush's 2001 tax cuts for the 2% of richest Americans (typically those earning more than $250,000) expire as scheduled at the end of 2010. Corporations will no longer be able to exclude foreign-source income from tax. Many popular tax deductions, such as those for local taxes, mortgage interest, health-care premiums and charitable gifts, will be limited for the rich. A yet-to-be-designed cap-and-trade programme for carbon emissions will raise additional revenue. To curb spending, Mr Obama promises to remove most American troops from Iraq before the end of 2010, reduce payments to privately managed Medicare plans and find other health-care savings.

Mr Obama told Congress in his address on the 24th that “everyone...will have to sacrifice some worthy priorities for which there are no dollars. And that includes me.” Yet the evidence of such sacrifice remains scarce. He appears to earmark his tax increases and spending cuts mostly to pay for his long-standing priorities: making permanent the worker tax credit in the fiscal-stimulus plan; expanding public subsidies for health care and college education; investment in alternative energy; and extra deployments to Afghanistan. And he suggested that he will need more money to bail out banks than the $700 billion already authorised. A $250 billion facility is being set aside for this, one reason why this year's deficit is so huge.

Most of Mr Obama’s targeted deficit-reduction comes not from his own actions, but from the expiry of the temporary stimulus, a halt to bail-outs, and the natural restoration of tax revenue as the economy pulls out of recession and grows by 2-3% over the next decade. And therein lies the biggest threat to the president’s plans. The economic outlook has darkened significantly even since January. Ben Bernanke, the Federal Reserve chairman, said this week that the recession would end this year only if the financial system stabilises, which so far it has not.



A longer recession or long-term stagnation pose two distinct fiscal risks. First, Mr Obama will be (rightly) reluctant to raise taxes, and tempted to extend parts of the stimulus package if unemployment is not dropping by 2010. Premature fiscal tightening, after all, could lengthen the recession, as Japan learned in the 1990s.

Second, a longer recession makes it harder for America to grow out of its debt burden as it, and other countries, have done at previous debt peaks. Because of stagnating output and declining prices, Japan’s nominal GDP in 2005 was smaller than in 1996, contributing mightily to a climb in that country’s net debt from 29% of GDP to 85% (it will reach 98% this year). One worrying parallel for America is that its nominal GDP will probably decline this year for the first time since 1949.

So Mr Obama’s 3% deficit target may be much harder to reach than he thinks; and it may not be tough enough anyway. Using reasonable policy assumptions, Alan Auerbach of the University of California at Berkeley, and William Gale of the Brookings Institution, think the deficit will bottom out near 5% of GDP in 2013 then climb to almost 6% by 2019, while debt continues to rise as a share of GDP. That is before the government has to deal with the full impact of the surge in health and pension entitlement costs. The academics reckon higher taxes or lower spending equal to a staggering 8% of GDP a year are necessary to contain those costs and stabilise the long-run debt.

Despite his inspiring rhetoric, Mr Obama’s plans for dealing with those long-term obligations have been frustratingly vague. He called on Americans to “address the crushing cost of health care” but proposes to spend many billions more, not less. He reportedly abandoned support for a commission to restore solvency to Social Security, the public-pension system, because congressional Democrats objected to this loss of their authority. He had a golden opportunity to introduce the idea of the rich, multinational corporations and carbon-emitters paying higher taxes as part of a broad reform of a monstrously inefficient tax system, and so make the economy more productive. He passed it up.

In fairness, these are early days in his presidency, and stabilising the economy needs to be his priority. The summit and the speech to Congress were just part of the essential process of softening up the public for the long, contentious chore of fixing entitlements and the tax system.

It was also an opportunity for Mr Obama to counter the pervasive economic gloom that he himself engendered with his warnings of “catastrophe” if his stimulus plan was not passed. With the rhetorical flair for which he is famous, he asserted that Americans would triumph because “amid the most difficult circumstances”—his voice briefly descending to a warm and coaxing growl—“there is a generosity, a resilience, a decency”. As if to prove his point, legislators gave one of their longest ovations to Leonard Abess, a Miami banker in attendance who sold most of his bank for $927 million and gave $60 million of the proceeds to 471 current and past employees. Even amid the gloom, there are occasional flashes of light.

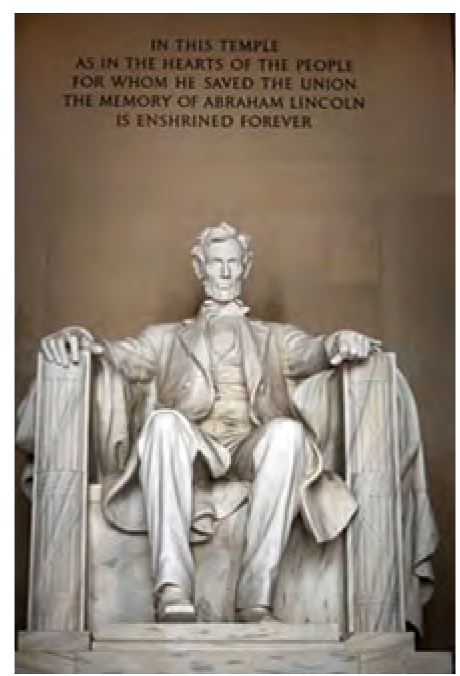
Voting rights for Washington, DC

A constitutional conundrum

Feb 26th 2009 | WASHINGTON, DC
From The Economist print edition

There's just one snag…

Reuters



He wants a vote

"I'M GOING to nail you here," an interviewer taunted Eleanor Holmes Norton, Washington, DC's, veteran congresswoman. "I checked your voting record. You have not voted once while you've been in office. Do you want to defend that?" The interviewer was Stephen Colbert, a comic. But his point was serious. The representative from the nation's capital can speak, but has no vote on whether bills become law. Ms Holmes Norton is not the only one who thinks that is unfair.

On February 24th the Senate voted to begin debate on a bill to enfranchise Washingtonians. A parade of senators called it "unimaginable" and "really astounding" that the 600,000 Americans who live in the district have no vote in Congress. If the bill passes the Senate intact, it should sail through the House of Representatives, and Barack Obama says he will sign it.

The snag is that the bill is unconstitutional. Members of the House of Representatives must be chosen "by the People of the several States", says the constitution. The District of Columbia is not a state, nor part of one.

The problem could be solved by amending the constitution, but this is hard. An amendment ratified in 1961 gave Washingtonians the right to vote in presidential elections. But a proposal in 1978 to give them representation in Congress was not ratified by three-quarters of the states, and so failed.

Another option would be to merge most of DC into a neighbouring state, such as Maryland, perhaps leaving only a rump of federal territory around Capitol Hill. That would give Washingtonians the same rights as other Americans. But they aren't itching to lose their independence. Nor are suburban Marylanders begging to have DC's urban problems dumped on them. And there is a bigger political game afoot.

Campaigners see a seat in the House as a first step towards statehood, or something like it. That would imply two new senators, giving DC, with 0.2% of the population, nearly 2% of the votes in the Senate. (Wyoming, though, has two senators, and even fewer inhabitants.) Since Washingtonians vote solidly Democratic, Democrats like this idea. Republicans, not surprisingly, are less keen.

The current Senate bill offers a compromise. Utah, a Republican stronghold with a growing population, gets another House seat to balance the Democratic gain in DC. Some Republicans are satisfied. Some think the party will do itself more harm than good if it opposes voting rights for a mostly black city. "It's an important civil right," Michael Steele, the party chairman, told the *Washington City Paper*.

But offering Utah another seat (which it could lose after the next census) does not resolve the constitutional conundrum. The courts may strike the bill down. And rule-of-law enthusiasts fret that if politicians do not feel bound by the constitution, there is no telling what they will do next.

Affirmative action

Erasing race

Feb 26th 2009
From The Economist print edition

Californian and Texan universities struggle with admissions policies

CALIFORNIA and Texas are both large states that are home to a growing population of minorities. They also share another trait. In a blow to the policy of affirmative action, public universities in the two states were forbidden, a decade ago, from using race as a factor in college admission decisions—by a federal court, in Texas's case, and by state law in California's.

Texas stalled, guaranteeing admission at the state university of his or her choice to any student graduating in the top 10% of their high-school class. This helped students from predominantly minority high schools who excelled relative to their peers. The University of California (UC), on the other hand, altered its admissions standards in 2002 to require a "comprehensive" review of applications. Under that system, students win points not just for academic criteria such as grades and test scores, but also for overcoming "life challenges". Affirmative action by the back door, some critics say.

Both policies have had modest success in maintaining diversity. But now policymakers in both states are about to shake the kaleidoscope again. William Powers, the president of the University of Texas (UT) at Austin, has sounded an alarm. The number of students in the top tenth of fast-growing Texas's high-school classes will have climbed from some 20,000 in 1998 to over 30,000 by 2015. Last year more than 80% of Texas freshmen at UT Austin came from this group. By 2013 it will be 100%.

Mr Powers has urged lawmakers to amend the law by capping the number of students who can be admitted under the rule at half of a state university's class. As for the other half, he wants the university to retain discretion over which students to admit, including the discretion to consider race. Without this change, Mr Powers says, the proportion of minorities at his university will decline: the top-10% plan yields only about 25% black and Hispanic students, but the university could admit far more if it retained control over the other half of its class. The Texas legislature almost passed such a change last year; a version of it is likely to pass this year.

Meanwhile, university officials in California voted earlier this month to overhaul their current admissions system, which guarantees a student a place at a UC campus if he ranks in the top 4% of his high-school class or in the top 12.5% of the graduating class statewide. The new plan alters the ratios so that the top 9% of students from each high school would be guaranteed a spot, as well as students who rank in the top 9% of the state as a whole. The overall effect is to make California's system resemble the system Texas now wants to give up.

This part of the California proposal has been met with little resistance. But a second aspect troubles critics of affirmative action. The plan would create a new category of applicants: those entitled to a "review" of their applications, though not to guaranteed admission. Under the new plan, students from roughly the top 20% of the state's graduating class would be required to receive a review of the "comprehensive" sort at any campus to which they chose to apply. University officials estimate that this entitled-to-review pool will contain more whites, blacks and Hispanic students, but significantly fewer Asians, than the pool of students currently eligible for admission. Critics have accused admissions officers of using the review process as a means to reinstate racial preferences in violation of the law. Nothing is ever easy.

Age and Californian cities

Gilded age

Feb 26th 2009 | SANTA BARBARA
From The Economist print edition

NIMBYs and old people make excellent defences against recession

THE lawns are green and well-tended. The swimming pools are filled with water, not mosquitoes. Steve Cushman, head of the local chamber of commerce, counts just 27 empty storefronts out of 410 along the city's main shopping street—a rate that many cities in California would envy. In the past year Santa Barbara County has seen a slight increase in employment. The secret to its health? Hostility to development and lack of youth.

Nowhere in California is immune to recession, but the oldest areas are proving most resistant. Of the ten counties with the lowest unemployment rates, nine, including Santa Barbara, contain an above-average proportion of people aged 65 or older. Youthful Los Angeles has shed almost a quarter-of-a-million jobs in the past year. Slightly older San Diego has lost a few thousand, while considerably older San Francisco has lost none. A map of the state's retirees (see above) could almost double as a map of economic resilience.

California's youngest regions are in its hot interior. In the middle years of this decade hundreds of thousands of families moved there in search of big, affordable houses. Unfortunately, many took on big, unaffordable mortgages to do it. Last month one in every 87 households in youthful, formerly fast-growing San Bernardino County received a foreclosure filing, according to California-based RealtyTrac. The housing crash has led such areas into an economic tailspin.

Santa Barbara has watched all this from the sidelines. In this slow-growth stronghold, anything other than a glacial pace of development is anathema. Mr Cushman says that only one block of flats for rent has been built in the region in the past 30 years. And some want to curtail growth further. Later this year the city will decide whether to reduce the maximum height of downtown buildings from 60ft to 40ft (18 metres to 12 metres). "We like Santa Barbara the way it is," says Marty Blum, the mayor.

This stuffy attitude has saved the city, together with others along the Pacific coast. Last month Santa Barbara County's foreclosure rate was just one in 298, well below the state average. Nor did the city build huge office parks which might now be vacant. As for industry, there was never much in the first place, "so there's just not much to lose," says Bill Watkins, an economist at the local branch of the University of California.

The diciest part of Santa Barbara's economy is the tourism business. Hotel receipts have dipped slightly this fiscal year as day-trippers from Los Angeles fasten their wallets. But much of the local economy is recession-proof. As well as the university, Santa Barbara has a large community college. It also has Cottage Hospital, which is being rebuilt—a job that will eventually employ up to 500 workers.

Health care is the only private-sector industry in California that accounted for job growth in 2008. Here, too, places benefit from having a fairly old population. The median age of people admitted to Santa Barbara's Cottage Hospital is 55—eight years older than UCLA Hospital in Los Angeles. Although hospitals complain it is too stingy, few sources of revenue are more stable than Medicare, which paid for 44% of Santa Barbara's patients in 2008.

In the past ten years, obedient to the findings of urban sociologists, American cities have tripped over themselves vying for young, creative people. They have revitalised downtowns and sponsored gay-pride parades. They might have been better off building retirement homes.

Judicial independence

Only in America

Feb 26th 2009 | CHICAGO
From The Economist print edition

The trouble with electing judges

AP



BACK in 1996, William Rehnquist, then chief justice of the Supreme Court, called an independent judiciary "one of the crown jewels of our system of government". He considered America's courts a model for other countries. Would-be foreign imitators might, however, consider *Caperton v Massey*, a case that the Supreme Court will hear on March 3rd. In 2004 Don Blankenship, the chief executive of Massey Energy, spent $3m to help elect Brent Benjamin to West Virginia's Supreme Court. In 2007 Mr Benjamin voted to overturn a $50m judgment against Massey.

With *Caperton v Massey*, the Supreme Court will consider the effect of campaign spending on the judiciary. Thirty-nine states hold judicial elections. The fights are bitter, part of an escalating war between business groups and trial lawyers. From 2000 to 2007 fund-raising for state Supreme Court races reached $168m, almost twice the amount raised in the 1990s.

The main question is whether Mr Benjamin's failure to recuse himself denied a fair trial for Hugh Caperton, whose coal company Massey had allegedly bankrupted through fraud. Rules for recusal do exist. The Supreme Court has warned against a "probability of unfairness", but its most definitive ruling only bars judges from cases in which they have a financial stake. Forty-seven states have adopted the American Bar Association's tougher rule for recusal when "impartiality might reasonably be questioned". But most judges are responsible for recusing themselves. Mr Benjamin thought it unnecessary.

Mr Caperton's lawyers argue that the nature of Mr Blankenship's spending, including its scale (60% of all the money raised for Mr Benjamin) and timing (Massey was preparing an appeal), created a "constitutionally unacceptable probability of bias". Mr Benjamin may, of course, have been truly impartial. But one poll found that 67% of West Virginians doubted it. Mr Caperton's cause has a wide range of supporters, from the Brennan Centre in New York to more unusual suspects, such as the Committee for Economic Development.

Reformers should temper their excitement. First, Mr Caperton may not win. Mr Blankenship was not, personally, a litigant and has done nothing illegal. He gave only $1,000 directly to Mr Benjamin's campaign; the rest came indirectly. The Centre for Competitive Politics, based in Alexandria, Virginia, filed a brief in the case that warns against restricting the right to free speech—in the past the Supreme Court has defended political spending under the first amendment. Mr Benjamin himself had no direct financial stake in the outcome of the case. He had ruled against Massey at least five other times, though in those cases his was not the deciding vote.

Second, even if the Supreme Court backs Mr Caperton, questions will linger. How much spending is too much? What about spending by chambers of commerce? States may consider reforms for recusal—some already are. But the Supreme Court in 1991 acknowledged “a fundamental tension between the ideal character of the judicial office and the real world of electoral politics.” As long as states elect their judges, that tension will remain.

Bad judges

The lowest of the low

Feb 26th 2009 | NEW YORK
From The Economist print edition

Another blow against elected judges

EARLIER this month, two judges in Pennsylvania's Luzerne County admitted sentencing thousands of children to jail in return for kickbacks from a prison-management company. Judges Mark Ciavarella and Michael Conahan received a commission for every day they sent a child to private juvenile detention centres run by Pennsylvania Child Care and a sister company. The pay-offs came to $2.6m over seven years.

“It just makes me think that anyone can betray the law,” says Jamie Quinn, one of the children exploited by the judges. Ms Quinn, from Scranton, was sent to juvenile prison for nine months at 14, after slapping a friend who, she claims, slapped her first.

Hillary Transue, who is 15 and faced Mr Ciavarella without a lawyer, was sentenced to three months because she constructed a fake MySpace page ridiculing the assistant principal at her high school. Her case led to the judges' downfall; children have a constitutional right to a lawyer, and the case first alerted Robert Schwartz, executive director of the Juvenile Law Centre. His organisation exposed the larger crime.

Adam Graycar, of the Rutgers Institute on Corruption Studies, explains that what is really unusual about this tale is the scale of the corruption. First the judges received monetary rewards for sanctioning the building of a new private-sector prison in their area. Second, they were paid for closing a county-funded prison nearby. And, then, of course, they offered up the “juvenile delinquents” for the benefit of the owners of the new jail. Both judges were elected, not appointed.

The judges are going to jail, but the prison companies have so far avoided prosecution. Mr Schwartz fears this is because Robert Powell, the former co-owner of Pennsylvania Child Care, has been co-operating with the authorities. If the prisons get off, though, that will be another disgrace.




Victory gardens

Digging their way out of recession

Feb 26th 2009 | LITTLE ROCK
From The Economist print edition

Allotments by any other name

IN 1943 Eleanor Roosevelt encouraged a return to the “victory gardens” that had become popular during the first world war, when the country faced food shortages. Mrs Roosevelt planted a garden at the White House; some 20m Americans followed her lead, and by the end of the war grew 40% of the nation’s vegetables.

Now a grassroots movement wants Barack Obama to plant another White House victory garden. The new secretary of agriculture, Tom Vilsack, announced recently that his department would create “The People’s Garden” out of a paved area outside their building. And he won’t stop there. Mr Vilsack wants there to be a community garden at each of the department’s offices around the world.

Margaret Lloyd, a researcher on victory gardens at the University of California at Davis, finds many reasons for this new national trend. The recession is one; but people are also worried about food safety, want to eat more healthily, and are bothered about climate change. This may be a way to make a difference.

If Washington needs further inspiration it might examine the movement in Bill Clinton’s former stamping-ground. Although Arkansas is an agricultural state, urban gardening has not always been popular. But now victory gardens are springing up in backyards, school grounds and even on front lawns in posh neighbourhoods. Many gardeners are focusing on “heirloom” plants—rare varieties from earlier times that do not appeal to agribusiness.

Classes are being offered on canning vegetables and raising chickens. The Station, a new grocery store about to open in Little Rock, will sell primarily local foods. Heifer International, a non-profit group that hopes to fight world hunger and poverty through self-reliance and sustainability, will host a conference in the city later this year to encourage the use of local produce in school cafeterias.

The two-acre Dunbar Community Garden in Little Rock has served as a model for several years. More than 600 students a month have learned about gardening there. The students can take these lessons home and recreate them in their own back yards. The garden, attached to an elementary and middle school, allows inner-city students to taste fresh-grown fruit and vegetables, sometimes for the first time in their lives. Produce grown in the summer months is sold to local restaurants.

Perhaps the most positive aspect of the garden movement comes from ventures like the Backyard Garden Project, which helps inner-city families start gardens for self-sufficiency. Ms Lloyd says that the most important promoter of projects like those in Little Rock should be Mr Obama. “It would be great to have a farmer-in-chief,” says Ms Lloyd. “It would set in motion something we as Americans can do in these tough times.”

Post-traumatic stress disorder

Take heart

Feb 26th 2009 | ST LOUIS
From The Economist print edition

PTSD sufferers deserve a medal

EVER since tribes of cavemen started throwing stones at each other, the wounds of war have been mental as well as physical. America's armed forces have long recognised the psychological damage war can cause. In the civil war, they called it soldier's heart; in the first world war, shell-shock; in the second, battle fatigue. Now it is known as post-traumatic stress disorder (PTSD).

A Pentagon study recently estimated that 11% of Iraq veterans and 20% of Afghanistan veterans suffer from PTSD. Another study counts some 300,000 victims in all. This is not a simple condition. Its effects can range from temporary readjustment problems to suicide and murder, both of which have reached alarming levels among soldiers returning from duty.

Although the armed services have promised a new commitment to treating PTSD, including opening new treatment centres at Fort Bliss, Texas and Bethesda, Maryland, ex-servicemen and their families say the government isn't doing enough. They blame a still-entrenched prejudice that psychological problems are a sign of weakness. But the fact that four suicides have occurred at West Point in the past seven months has prompted the army to promise that seeking help will not endanger a soldier's career.

Last year Robert Gates, the defence secretary, opened the possibility of honouring PTSD sufferers with the Purple Heart, a medal created by George Washington which is awarded for wounds received in combat. After heated debate, the Pentagon recently announced that it would not do so. This maintains the standard set in 1932, which awards the Purple Heart to those who have suffered wounds "intentionally caused by the enemy from an outside force".

Most veterans' organisations applauded the decision. But some of those who have served in Iraq and Afghanistan object that their shattered lives are as real as any physical wound and just as deserving of honour. Like trauma to the brain—the most typical wound of the Iraq war, which sometimes cannot be detected with a CAT scan—PTSD is undeniably real.

The debate is sure to continue. Advocates of honouring PTSD-afflicted soldiers expect that it will take a cultural change in attitudes about mental health before the victims are acknowledged. That will take some time; the Pentagon moves slowly. Veterans of the cold war are still doggedly pursuing their own service medal. And by the time the memorial in Washington, DC, to the soldiers of the second world war was completed in 2004, many of "the greatest generation" had already died.

Lexington

Californication

Feb 26th 2009
From The Economist print edition

America has witnessed a huge shift in regional power

Illustration by David Simonds



THE 2008 election did not just put a new president in the White House. It also completed one of the biggest shifts in the regional balance of power in America's recent history, draining influence away from the once-mighty South and redistributing it to the coasts. This will help determine who gets what from Barack Obama's attempts to stimulate and reshape the economy.

The biggest winner from this internal revolution is America's biggest state, California. Nancy Pelosi, who has been speaker of the House since 2007, is no longer restrained by a Republican president. Californians run two of the most powerful committees in the House: Energy and Commerce (Henry Waxman), Education and Labour (George Miller), plus an important subcommittee on intelligence (Jane Harman). Most of the Californians act as Mrs Pelosi's praetorian guard in the House, not least because she sometimes gives them a lift home on her official jet.

Two of the most powerful voices in the Senate, Dianne Feinstein and Barbara Boxer, are also Californians. Mrs Boxer has already made it clear that, as chairman of the Environment and Public Works Committee, she will do her best to improve California's crumbling roads. And Mrs Feinstein, who runs the Intelligence Committee, has already given Mr Obama a flea in his ear for not consulting her before nominating Leon Panetta to run the CIA.

Californian number-plates will not be as ubiquitous as Texan ones used to be in the White House car park. But Mr Obama has nominated several Californians to leading positions in his administration besides Mr Panetta: Hilda Solis, a former congresswoman, to run the Labour Department, Steven Chu, a former head of the Lawrence Berkeley National Laboratory, to Energy, Nancy Sutley, a former deputy mayor of Los Angeles, to run the Council on Environmental Quality.

The rise of California is matched by the fall of the South. Southern politicians have long punched above their weight in Washington. Southern Democrats such as Lyndon Johnson and Sam Rayburn dominated Congress before the civil-rights era. The rise of the modern Republican Party projected a succession of southern conservatives to the pinnacle of power—Newt Gingrich and Dick Armey in the 1990s and Tom DeLay in the early 2000s; not to mention the two Texan George Bushes. The Democrats were so worried about their decline in the South that they ran two southerners, Bill Clinton and Al Gore, in 1992 and 1996. Now the South is as impotent as it has been for a century.

This geographical shift has brought dramatic changes in style and substance. California's Democratic House delegation is the most diverse on the Hill, with 10 white women, nine Hispanics, four black women and two Asian-Americans. It is also one of the most left-wing, according to the voting records. It is hard to imagine a bigger change from the southern-fried conservatives who once lorded it over Congress.

Equally striking is the social difference between the Californians and the southerners. Mrs Pelosi, Mrs Feinstein and Mrs Harman are all married to wealthy businessmen—extremely wealthy in Mrs Harman's case. Mrs Pelosi's district, San Francisco, is a combination of a playground for the ultra-rich and a sewer for the underclass, with the middle classes priced out of the market. Mr Waxman's district, West Los Angeles, is the glitziest concentration of wealth on the planet. The southerners, by contrast, were mostly men of modest means who represented middle-class suburbs, a world away from Pacific Heights, where Mrs Pelosi lives, and Rodeo Drive, in the heart of Mr Waxman's district.

The Californian Democrats' agenda is the polar opposite of the southern Republicans': pro-green and pro-union, anti-business and anti-war. Mr Waxman and Mrs Boxer have long outdone most of their party in supporting tougher environmental standards. As the architect of much of the anti-tobacco legislation of the 1990s, Mr Waxman is casting around for new monsters to slay. (High on his list are energy companies.)

A dangerous state

The Californication of the Democratic Party carries all sorts of risks. The most obvious is that California has the most dysfunctional politics in the country. The Golden State has one of the highest unemployment rates in America, at 9.3%, thanks to its high taxes, its unions, its anti-business climate and its gigantic housing bubble. Some 100,000 people have fled the state each year since the early 2000s. More would follow if they could sell their houses. A second risk is party disunity. The rise of the Californians has already produced bloodshed: Mrs Pelosi beat Martin Frost, a Texan moderate, for the leadership, and Mr Waxman dethroned John Dingell, from Michigan, for the chairmanship of the energy committee. Sherrod Brown, a senator for Ohio, and Debbie Stabenow, a senator for Michigan, have both worried aloud about overzealous environmental legislation and the coastal bias against manufacturing.

The biggest risk is overreach. Many Californian liberals are as far to the left on cultural issues as the southern Republicans were to the right. Many of them also draw their support from two groups that have limited appeal to the rest of the country, particularly to the "bitter" voters that Mr Obama had such trouble wooing in November; the fabulously rich and public-sector activists.

All this suggests that one of Mr Obama's most delicate tasks, if he wants to prevent his party from being captured by the "left coast" in the same way that the Republicans were captured by the South, will be to contain the Californian barons. He has plenty of advantages when it comes to performing such a task. Chicago is not San Francisco. And Mr Obama did remarkably well in the South, capturing Virginia and North Carolina and coming within five points of taking Georgia. But putting just one person with a southern drawl in his cabinet might have helped.

The Brazilian Amazon

Preventing pillage in the rainforest

Feb 26th 2009 | BOA VISTA, RORAIMA STATE
From The Economist print edition

A scheme to regularise land holdings in the Amazon forest faces many obstacles

Still Pictures



GRAND plans to halt the destruction of the Amazon rainforest have come and gone over the years with scant success, so a degree of scepticism about Brazil's latest scheme seems justified. However, one positive sign is that, this time, the federal government seems to have recognised the importance of working with, rather than against, state governments in the region.

The new plan, discussed at a meeting of state governors and federal officials earlier this month, involves regularising the titles to 80% of the private land holdings in Brazilian Amazonia over the coming three years. This, it is hoped, will encourage the occupants to stay and improve their land instead of abandoning it and moving on to clear the next patch of virgin forest.

A small-scale initiative under way near the village of São Luiz do Anauá in Roraima state provides an illustration of what the scheme hopes to achieve. The local soil is the colour of cement and almost as rich in nutrients. The area was deforested 15 years ago. Cattle ranchers came and went, and for the past few years the land has been unproductive. But now, neat rows of palms sit waiting to be planted, thanks to a biofuels company based in São Paulo.

Brazil lacks a central land register, suffers widespread forgery of title deeds and has a long history of squatters seizing land. A widely-quoted study by Imazon, an NGO, reckoned that only 4% of private land in Amazonia is covered by secure title deeds. Much of the rest has been grabbed in the hope of establishing de facto ownership eventually.

The government's new scheme is, in principle, simple. Plots of up to 100 hectares (247 acres) will be given to the people farming them. Larger ones, of between 100 and 2,500 hectares, will be sold using various different pricing mechanisms. Plots of over 2,500 hectares will be reclaimed by the government, which is meant to own them anyway. Roberto Mangabeira Unger, the minister responsible for the new scheme, believes that solving the problem of insecure land title will "change the economic equation that has made pillage more attractive than either preservation or production in the Amazon."

In the past, however, similar initiatives have floundered, for a number of reasons. First, state and federal governments have disagreed over who should be responsible for what. The state governors particularly dislike INCRA, a federal agency charged with distributing small plots of land. Eduardo Braga, the governor of Amazonas, says "INCRA abandoned the families it settled on land in the Amazon without

electricity or infrastructure.” The agency certainly has a poor record of preventing deforestation on the land it administers.

Second, the existing laws that govern what land can be used and what cannot are confusing and close to unenforceable. In the 1960s and 1970s, farmers were sometimes required to cut down trees as a condition for getting credit from the state. Some token efforts were made to change this regime in the 1980s, and then in 1996 a decree was issued requiring 80% of each plot of land to be preserved as forest, with only 20% to be cultivated or ranched. This law is widely ignored, and when the government has tried to enforce it, it has often met with strong resistance from the men with the chainsaws. Given this history of mutual antagonism, the process is unlikely to be smooth.

Still, some of these problems have been resolved in the new plan, which has the force of law via a presidential decree. On a federal level, the Ministry for Agrarian Development will handle some of the implementation, taking it away from INCRA, which could be described politely as troubled. Mr Unger, a former Harvard law professor, seems to have succeeded in charming the governors of the states in the Amazon into a more co-operative mood. “We have Obama’s teacher here,” says José de Anchieta Júnior, the governor of Roraima, while addressing a public meeting in the state. “Things are looking up.”

Nevertheless, there is a risk that the scheme, by making it easier to get secure title for dubious land claims, might somehow stimulate demand for virgin forest land, not damp it. And, as ever, enforcing the rules will be the difficult bit. President Luiz Inácio Lula da Silva’s government has shown an indulgent attitude to violations of property rights elsewhere in the country by the Landless Movement, making it an unlikely guardian of them now. The new scheme is not bound to fail, but the sceptics will take a bit more convincing.

Quebec

Fighting old battles

Feb 26th 2009 | MONTREAL
From The Economist print edition

A 250-year-old defeat still rankles

THE Battle of the Plains of Abraham was brief and not all that bloody, but it was historic. On September 13th 1759, France's loss of its colonial territories in North America was set in motion when British redcoats scaled cliffs protecting Quebec City and defeated troops and militia loyal to Louis XV. A modern-day battle over the battle, which concluded on February 17th, lasted somewhat longer and ended very differently. It flared up over plans to mark the battle's 250th anniversary with a re-enactment, and ended with Quebec separatists crying victory and Canada's federal government beating a hasty retreat.

The re-enactment was to have been the centrepiece of a summer-long commemoration of 1759's events. But to some Quebeckers commemoration sounded like celebration. "Dancing on the graves of our ancestors," was how the Réseau de Résistance du Québécois (RRQ), a group of sovereigntist hardliners, described it. They demanded the re-enactment's cancellation. For several weeks debate raged. The re-enactment was an exercise to pay tribute to the fallen and educate the living about one of Canada's most important episodes, said its supporters. These included 2,000 or so mostly American "re-enacters", the federal government and Quebec City's mayor, who was loth to lose millions of dollars in tourist spending.

Opponents, and most of the French-language press, cursed the proposed re-enactment as a "repugnant federalist propaganda operation". When it reached a point where its organisers were receiving threats—including having "our bayonets shoved up our butts", according to their leader—the National Battlefields Commission, which administers the Plains of Abraham, cancelled the mock battle and other activities planned for the summer. Or, as the *Gazette*, Quebec's only English daily, wrote, it "cravenly surrendered the field".

If there was an edifying component to the brouhaha, it lay in displaying the different light in which the Conquest, as it is known, is seen by those on opposite sides of the Quebec independence debate. For many sovereigntists it was the beginning of domination by the wretched English, and of the struggle for cultural survival. Federalists, however, both Francophone and Anglophone, argue that after the Conquest the French of New France got rights they could only dream of under the exploitative, authoritarian *ancien régime*.

Whatever the case, the re-enactment was probably doomed from the moment in mid-January when the RRQ pledged "to go on the warpath" against it. Support for Quebec's sovereignty spikes whenever it is felt that English Canada is taking it for granted or not respecting it. Wise federal politicians are thus wary of anything that may rile Quebec sensitivities. Nevertheless, a few cabinet ministers took opposing positions on the re-enactment.

Quebec's premier, Jean Charest, was shrewd enough not to get involved. He simply announced that he would not attend. This is a decision Generals Wolfe and Montcalm, the commanders of the British and French forces in 1759, should probably also have made; both died of wounds suffered on the Plains of Abraham.



Colombia

Spies in trouble

Feb 26th 2009 | BOGOTÁ
From The Economist print edition

The domestic-intelligence agency is caught misbehaving again

IN COLOMBIA most politicians, senior officials, opposition figures, business leaders, journalists and of course suspected drug-traffickers and leftist rebels have long been careful about what they say over the telephone, assuming that someone is recording their conversations, legally or otherwise. Their suspicions, it turns out, were justified.

An investigation by a news magazine, *Semana*, found that domestic-intelligence officers had been intercepting the phone calls and e-mails of dozens of public figures, including Supreme Court judges and President Álvaro Uribe's private secretary, without court orders.

Semana said the group of intelligence officers was intercepting the messages in exchange for cash. Government spokesmen say they were part of a drug-trafficking-related mafia that has infiltrated the intelligence agency. But critics say only the government would be interested in the phone conversations of opposition figures. They suspect that senior officials ordered the taps.

Either way, the scandal at the Administrative Security Department (DAS) casts a cloud over Mr Uribe's tough but successful security policies, which have pushed leftist rebels far from urban centres and restored government control over much of the country. The DAS answers directly and exclusively to the president. Under Mr Uribe, who has been in power since 2002, it has been a maelstrom of criminal infiltration and scandal.

Mr Uribe's first DAS chief, Jorge Noguera, is in jail and facing conspiracy charges for allegedly colluding with right-wing paramilitaries and providing them with information on union activists who were later targeted for assassination. Another DAS director resigned in October 2008 when it was revealed that one of her intelligence officers had issued a directive ordering the surveillance of Gustavo Petro, an opposition senator. The current director, Felipe Muñoz, has been at the job only a month and, according to the magazine's investigation, many of the agency's illegal recordings and files were destroyed before he took office.

But the DAS is only one of several Colombian agencies equipped to eavesdrop. The national police, which comes under the defence ministry, was hit by a similar scandal in 2007, when 12 senior officers were forced to retire after another illegal wiretapping ring was uncovered.

Uncharacteristically, Mr Uribe has issued only a brief statement since the latest scandal broke, saying he did not order the wiretaps and claiming to be a "victim of this infamy."

So far, the deputy directors for counter-intelligence, analysis and operations at the DAS have been fired in what will probably be another big shake-up at the agency. The defence minister, Juan Manuel Santos, one of Mr Uribe's most loyal lieutenants and a possible candidate to succeed him—if, that is, Mr Uribe decides not to seek a third consecutive term in 2010—was in Washington for meetings with members of President Barack Obama's cabinet when the scandal broke back home. Mr Santos was one of the government officials targeted in the taps; he suggested that the DAS be abolished and replaced by a new and leaner civilian-security agency.

He will probably face some tough questions from American officials about the latest spying episode, as the Obama administration weighs the future of a $500m annual aid package that America has been giving Colombia for nearly a decade. Among the billions of dollars in aid, America has provided eavesdropping equipment to Colombian security forces for the "principal, fundamental and sole" objective of combating drug trafficking and terrorism, said America's ambassador to the country, William Brownfield.

A Colombian government spokesman said dismantling the DAS was not under consideration, but that a complete overhaul was planned. Three years ago, after Mr Noguera, its then chief, was charged with putting the agency at the service of paramilitary warlords, a special commission made a series of recommendations to clean up the organisation, but few of these were implemented. According to a commission member, Carlos Gustavo Arrieta, if even some of the measures had been put in place, “We might not have ended up where we are today with this.”

The Stanford affair

An $8 billion scandal goes a long way

Feb 26th 2009 | PORT OF SPAIN
From The Economist print edition

The allegation of an $8 billion fraud against Sir Allen Stanford is causing financial worries across the region, not least in Antigua, home to his main bank

AFP



Will they get their money back? And whom will they blame?

AFTER years of hobnobbing with international sports stars, Sir Allen Stanford, a financier accused by American authorities of an $8 billion fraud, now seems short of friends. But Lester Bird, Antigua & Barbuda's opposition leader and former prime minister, still has kind words. "Stanford has done a lot for this country," he told the local *Daily Observer,* calling Sir Allen's indictment "spurious".

Sir Allen's businesses dominate the Caribbean country of just 85,000 people. Besides his Stanford International Bank—at the centre of the alleged fraud—and the smaller Bank of Antigua, he owns a property company, two restaurants, a cricket ground and the *Antigua Sun* newspaper. On February 20th, the day after America's FBI found Sir Allen near Washington, DC, and took his passport, Antiguan regulators and the Eastern Caribbean Central Bank seized his financial interests in Antigua.

Across the Americas, from Quebec to Quito, investigations were launched into local offshoots of the Stanford group while investors tried, mostly in vain, to get their money out. Richer people in Latin American and Caribbean countries had poured their savings into Sir Allen's offshore schemes, seeking protection from instability at home (or for less laudable motives). In Venezuela investors are thought to have over $2 billion in Stanford-linked firms.

Political as well as economic consequences are bound to follow in several countries, especially Antigua. Shortly before the affair broke, the prime minister, Baldwin Spencer, was bringing forward his plans for an election amid rumours that Mr Bird and his Antigua Labour Party (ALP) were seeking Sir Allen's financial help to make a comeback.

Now Mr Spencer will have to seek re-election in the wake of a financial collapse whose effects on his country he says will be "catastrophic". As US marshals raided Sir Allen's offices in Texas on February 17th, Mr Spencer announced that the poll would be held on March 12th.

Long before a date had been set, campaigning had started, with hot-tempered allegations of trickery flying freely. Mr Bird and several of his former ministers face corruption charges relating to events during their long stay in office. Mr Bird's father, Vere Bird, dominated local politics, apart from one five-year break, from 1951 to 1994, when his son took over the family firm.

Both the ALP and Mr Spencer's United Progressive Party (UPP) have had dealings with Sir Allen. Mr Spencer's finance minister, Errol Cort—who had switched sides from the ALP—announced a "far-reaching and historic alliance" with the financier in his first budget, in 2004. Sir Allen's firms promised to write off $18.5m of government debt and pay for educational projects. In return, he got official backing to develop a huge tourist resort (which remains unbuilt). But the friendship turned sour. In 2007 Mr Spencer denounced Sir Allen's "haughty, arrogant and obnoxious behaviour". Sir Allen retorted that he had given his "heart and soul" to Antigua.

Whereas Mr Spencer and the UPP merely accommodated the country's biggest investor, the ALP had nurtured him. The Vere Bird government welcomed an as-yet unknighted Mr Stanford to Antigua in the late 1980s after the authorities in the British overseas territory of Montserrat closed his offshore bank. His Antiguan operations prospered, although the country's growing offshore industry suffered various scandals and two blacklistings by foreign regulators.

The *Antigua Sun* gave loyal coverage to the ALP and Mr Stanford made donations to its candidates. By 1999 he was an Antiguan citizen and a free-handed lender to a cash-strapped government. By 2004 it owed Stanford companies $85m, over 10% of GDP. Two years later, on the recommendation of the ALP, by then in opposition, Mr Stanford was knighted.

Some of his ventures did not prosper. In 2003 he promised a $2 billion Stanford Caribbean Investment Fund, which came to nothing. Two Stanford-owned airlines closed in 2007, and a promised merger involving a third airline never materialised. The star-studded Stanford cricket board was dissolved last December, and in January his property company laid off around 200 staff.

Antiguans, like Peruvians, Venezuelans and others affected by the affair, are long accustomed to public scandal. Normally, allegations against politically connected financiers elicit little more than world-weary sighs. But this affair, besides its spectacular scale, coincides with slumps in tourism and natural resources, the mainstays of the region's poorer countries. It could hardly have come at a worse time.

Correction: Brazil

Feb 26th 2009
From The Economist print edition

Correction: In our February 14th edition we said Brazil's oil and gas output would rise to 5.7m barrels' equivalent a day by 2020. The figures in the chart and text were in fact for Petrobras. Sorry.

China and Tibet

Not much of a celebration

Feb 26th 2009 | TONGREN AND XINING
From The Economist print edition

The new year arrives in Tibet with the region under armed guard

AP



IN TIBET, March is the cruellest month, the traditional season for doomed protests against Chinese rule. This year the authorities are unusually edgy. They have mounted a pre-emptive clampdown of a severity rarely seen in recent years. Monastery towns across a wide area of the Tibetan plateau are being sealed off from visitors. In those still accessible, troops are on heightened alert to prevent any repeat of last year's explosion of discontent.

Security measures vary across the vast Tibetan-inhabited area of China, which includes parts of four provinces as well as the Tibet Autonomous Region itself (see map below). Helmeted troops bearing rifles patrol Lhasa, the Tibetan capital. Snipers lurk on rooftops near the Jokhang temple, Tibet's holiest shrine and often a focus for protests. A Western tourist says she was conspicuously followed by plain-clothes police during a recent trip. Foreign journalists are largely barred from Tibet. Chinese travel agencies say foreign tourists are also denied entry until late March.

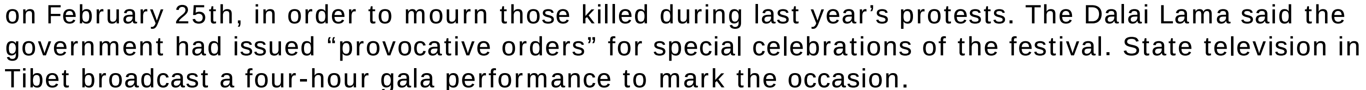
In recent days troops have been blocking approach roads to Tibetan areas in Gansu and Sichuan. They look like members of China's paramilitary People's Armed Police (PAP), but many Tibetans believe that regular army soldiers dressed in PAP uniforms are involved in the operations as well. One source says that army barracks across the plateau have been busy building extra accommodation in recent months to house an influx of soldiers.

Tense anniversaries in March include the first of rioting in Lhasa last year, and the 50th of both the uprising that led to the Dalai Lama's flight to India, and, on March 28th, of the replacement of the local government in Tibet by one more tightly under Communist control. The government has said this date will be officially marked as Tibet's "liberation from serfdom". Few Tibetans will be joyful.

The mood has been soured by widespread arrests in the wake of last year's unrest. International Campaign for Tibet (ICT), an NGO based in Washington, DC, says official figures suggest that some 1,200 of these detainees remain unaccounted for. More than 70 have been given prison sentences. There have been abundant reports of torture and other mistreatment.



Even so, fresh unrest has been reported in recent days by Western human-rights groups. On February 15th police took away a lone monk who protested in the town of Litang in Sichuan. The next day a small group of Tibetans who gathered to demand his release were also seized. On February 19th a crowd reportedly set fire to police vehicles in Nagqu after a fight between a Tibetan and a Han Chinese taxi driver.



Tensions have also been stoked by appeals from Tibetans abroad to avoid celebrations of the Tibetan new year, which this year fell on February 25th, in order to mourn those killed during last year's protests. The Dalai Lama said the government had issued "provocative orders" for special celebrations of the festival. State television in Tibet broadcast a four-hour gala performance to mark the occasion.

But in Qinghai, which was also swept by protests last March, the authorities in some areas have refrained from the all-out campaign under way elsewhere to eliminate open displays of loyalty to the Dalai Lama. In Tibet, monks have been ordered to take part in "patriotic education" meetings involving denunciation of their spiritual leader. This was common even before last year's unrest, but ICT says that this time ordinary citizens have been required to take part in such exercises. A meeting in Lhasa last month presided over by Zhang Qingli, Tibet's Communist Party chief, called on security personnel and the public to "smash the furious assaults of the Dalai Lama clique", a reference to claims that the Dalai Lama has been fomenting unrest.

In Rongwo monastery in Qinghai's Tongren county, however, pictures of the Dalai Lama are on conspicuous display in many of the shrines. One prayer room centres on a large and elaborate portrait of him in silk embroidery. Banknotes placed as offerings cover a small table in front. Several pictures can also be seen around the monastery of the boy recognised by the Dalai Lama in 1995 as a reincarnation of the Panchen Lama, Tibetan Buddhism's second-highest figure. China refused to accept him, keeping him hidden and appointing its own candidate as Panchen Lama instead. Shops near Rongwo monastery openly sell pictures of the Dalai Lama and of the Karmapa Lama, leader of another important branch of Tibetan Buddhism, who fled to India in 1999. At an internet café, Chinese visitors can read foreign websites about Tibet's hierarchy-in-exile. At Kumbum monastery, near the provincial capital, Xining, monks say they have not had to denounce the Dalai Lama.

Many of Rongwo's monks were detained after last year's protests. Some monks, at least, say that all are now free again, after, in a few cases, several months in custody without trial. PAP troops occasionally patrol the streets, but with soft hats and carrying batons and shields rather than guns. On Tibetan New Year's Day monks chanted prayers, with little sign of tension. But a Tibetan restaurant owner complains that calls for a subdued new year kept away dance troupes and the custom they would normally attract.

Officials are unlikely to conclude, however, that a lighter touch is any more effective than Lhasa's iron fist. Protests last year broke out both in tightly controlled areas and in parts ruled less aggressively, and in relatively affluent districts as well as poorer regions. Woeser, a Tibetan poet and blogger, says that some ethnic-Tibetan officials privately complain about the clampdown, but Han Chinese officials in Tibet toe a uniformly hard line. Officials in Beijing worry about Woeser too. Her blog, strongly sympathetic to Tibetan sufferings, is blocked in China. She says police have been deployed outside her Beijing home and follow her when she goes out.

However Tibet weathers the upcoming protest season, it will be a tough year of the Earth Ox. Tourism, a pillar of the Tibetan economy, has been devastated by the clampdown. Chinese citizens are much freer to visit than foreigners, but many are apparently fearful of going. For their part Tibetans complain that they are now treated elsewhere in China almost as terrorist suspects. Hotels refuse them rooms and Han Chinese mutter about "separatists". China's crackdown, however mildly or fiercely imposed, is breeding resentment and storing trouble for the future.



WORLD
ASIA

China and the Dalai Lama

Politically incorrect tourism

Feb 26th 2009 | HONG YA, QINGHAI
From The Economist print edition

A pilgrimage to the birthplace of a jackal in monk's clothing



ON THE eastern edge of the Tibetan plateau lies a shrine that, according to China's propagandists, should not exist. The house where the 14th Dalai Lama was born in 1935, under the name Lhamo Thondup, is tricky to find. It is tucked away in Hong Ya, a mountain hamlet of 200 people, which merges with the dusty crags to which it clings. Worshippers and tourists are not deterred. They seek out a pair of wooden doors with white prayer scarves draped through iron knockers. Inside, they pay their respects to a man China reviles.

The residence, with its throne room and prayer wheel spinning next to a portrait of the exiled leader, is a curious anomaly. It is there by Chinese government design. A casualty of the Cultural Revolution, it was rebuilt in 1986 when China was negotiating with the Tibetan government-in-exile. Xinhua, the official news agency, reported that it cost 350,000 yuan ($51,000) to resurrect, and boasts 61 rooms. In fact, there are six at a push. One stores a motorcycle.

Its status has changed from propaganda tool to unofficially sanctioned tourist spot (popular with Japanese tour groups) and discreet prayer site. The house is looked after by Gonpo Tashi, a distant cousin of the Dalai Lama. A tidy government wage of 3,000 yuan a month for his dual roles as village head and school headmaster helps him guard the Dalai Lama's legacy. He charges tourists a 20-yuan entrance fee. Despite last year's unrest, he won permission for a new building to house the main shrine. It now stands in the courtyard, painted brilliant yellow and topped by a gilded roof.

The shrine is tolerated because Hong Ya is an unlikely focal point for Tibetan resistance, high above a valley dominated by Chinese Hui Muslims. Hardly any locals call it Takster, its Tibetan name. Although 70% of the population is ethnically Tibetan, no one speaks Tibetan fluently. When the Dalai Lama was born, the region, regarded by Tibetans as part of Amdo, a province of their historic homeland, was under the control of a Muslim warlord, Ma Bufang. The Dalai Lama and his family didn't learn Tibetan until they moved to Lhasa in 1939.

Periods of tension require tiptoeing. The road to Hong Ya was blocked by police last March after riots by Tibetans. A recent visit confirmed it was open again. Gonpo Tashi's wife was showing round a well-heeled Tibetan couple, their hands clasped in prayer. A foreigner was not welcome. She whispered that her husband was next door with the local government boss. “Please leave or we'll get into trouble,” she pleaded.



The yakuza

Feeling the heat

Feb 26th 2009 | TOKYO
From The Economist print edition

The cops are squeezing the robbers

Illustration by Claudio Munoz



"IN THE old days," laments the retired mobster, with a broad smile, slicked hair and a heavily tattooed body, "the *yakuza* served a useful purpose in society to solve civil disputes and keep the streets clean." He draws on his cigarette, the stub of an amputated little finger visible in his beefy hand. "Now", he goes on, "it has lost its *samurai* spirit to moneymaking."

Or perhaps, the *yakuza*—Japan's organised-crime groups that date from the 17th century—are getting squeezed. For most of the post-war period they operated openly: tolerated by the public, used by politicians and protected by police. Crime will happen anyway, went the argument, so better to know whom to call when it crosses the line. In the 1950s ministers and industrialists relied on the mobsters and nationalist groups to quash unions and socialists. The gangs upheld classic Japanese virtues of manliness and loyalty—and paid for mistakes by slicing off one of their fingers in atonement.

But this orderly way of life is fraying. The floundering economy has eaten into revenue from traditional activities that required muscle, such as gambling, prostitution and loan-sharking. To compensate, the groups have ploughed into financial fraud, stock manipulation and cybercrime, giving rise to a new generation of gangster-nerds, more interested in business than blackmail. Still, the *yakuza* boasts 84,000 members (of whom half are "part-timers") and is estimated to haul in as much as ¥2 trillion (around $21 billion) annually.

Moreover, the public has become slightly less accepting after bouts of mob violence, traditionally hidden, that claimed innocent lives. On February 20th around 160 people from Tokyo's Akasaka district sought a court injunction to bar Inagawa-kai, a big crime syndicate, from occupying an office building, arguing that it might bring violence to the area. In August residents of the city of Kurume sought a similar injunction against a local gang.

A 1992 anti-mob law clearly defined illegal behaviour and penalised companies with *yakuza* ties. It also established a non-profit group called the National Centre for the Elimination of Boryokudan (crime syndicates), to advise companies on avoiding the *yakuza* and rally citizens to complain, as in the recent suits. But the law is not all that it seems. The nationwide centres it created, grumble both senior police and racketeers, provide lucrative sinecures for retired police officers. This recalls *amakudari*, or "descent from heaven"—the practice of rewarding government officials with cushy, post-retirement jobs in the area of their official responsibility.

Companies are "encouraged" to donate to the centres, and to hire retired officers to help them comply with the law. Owners of *pachinko*-parlours (venues for a popular sort of pinball) and others now hire security firms using former policemen. Having *yakuza* at the door invites trouble with the law. So companies are, in effect, paying off the cops rather than the mob.

Many bars and restaurants still prefer the *yakuza* to the police for handling troublesome customers. The service is better. Still, the breakdown of the traditional order irks the former crime boss. Pondering the changes, he uses the word *natsukashii* (nostalgia), as the smoke from his cigarette wafts into nothingness.



WORLD
ASIA

Cambodia's oil resources

Blessing or curse?

Feb 26th 2009 | PHNOM PENH
From The Economist print edition

Waiting for the oil (and money) to flow

MANY countries have been afflicted by a "resource curse". Discoveries of oil or other mineral deposits are hailed as offering a way out of poverty. But hopes are dashed as corrupt officials pocket the money or squander it on grandiose projects. Cambodia, giddy at the prospect of an oil boom, hopes not to go the same way.

A recent report, called "Country for Sale", by a London-based NGO, Global Witness, points out that amendments to a 1991 law had the effect of placing the Cambodian National Petroleum Authority (CNPA), the body administering oil contracts, under the direct control of Hun Sen, the prime minister, and Sok An, his deputy. It alleges that millions of dollars paid to the government to secure oil concessions do not show up in the official annual revenue reports. Meanwhile, unrestrained mining exploration has seen thousands forcibly evicted from their land in the north, and has damaged six of the country's 23 protected wildlife areas.

The discovery of oil and other minerals was a godsend to Cambodia. Despite foreign-aid donors' constant pleas for restraint, logging companies have largely exhausted the country's once abundant forests. Chevron, a California-based oil giant, at first estimated its 2005 oil discovery in the Gulf of Thailand at 400m barrels, enough to earn about $1.7 billion a year, against the government's budget last year of $1.2 billion. Chevron was awarded the largest exploration contract in the block thought to be most productive. But it has found that the oil is scattered in pockets and hard to extract. Despite the recent fall in the oil price, the government still hopes production will start in 2012.

It will be very welcome: aid still makes up half of the government's budget, despite a decade of stalling on anti-corruption legislation that donors want to see. The World Bank consistently ranks Cambodia in the bottom 10% of all countries for controlling corruption. Michael McWalter of the Asian Development Bank, who advises the Cambodian government on oil, argues that the CNPA is underfinanced and ill-equipped to deal with the complexities of the oil business.

In March last year the United Nations Development Programme and the Norwegian government jointly organised a conference to discuss what the government should do. The advice included the creation of an independent, transparent oil fund. This however, was largely based on the experience of Norway, which has an effective system of checks and balances.

Cambodia does not, and Mr Hun Sen and Mr Sok An have still not come up with a coherent plan for managing the oil revenues. According to Global Witness, the government decided at a meeting with donors in October not to join the Extractive Industries Transparency Initiative (EITI), an international coalition that would require full disclosure of oil, gas and mining revenues. Rather, it agreed to endorse only the principles underpinning the EITI, making its rules non-binding.

Government officials have responded to the allegations by lashing out at NGOs. At a conference in February, Mr Hun Sen called NGOs' criticism of his oil policies "crazy". And he has already alluded to the prospect that oil revenues may diminish the influence of aid donors—though he denies they have much anyway, since Cambodia can always turn to China, a generous donor, which, he says, despite its might, treats its partners with respect.

Bangladesh's economy

No hiding place

Feb 26th 2009 | DELHI
From The Economist print edition

A battered economy takes another hit

POLITICAL instability, natural disasters, and corrupt politicians: Bangladesh's economy has withstood a lot in recent years. But the global economic crisis will test its resilience as much as any of its traditional afflictions. Both its main sources of foreign exchange, workers' remittances and garment exports, are at risk.

By January 2007, when the army stepped in to install a two-year interim government of unelected technocrats, Bangladesh had topped international corruption rankings for five consecutive years. Yet the economy had grown at more than 6% a year since 2004, and poverty had fallen faster than ever. Donors called it the "Bangladesh paradox". Of course, no one ever believed in such a paradox. It was a polite way of telling politicians that the country could do even better if they kept their hands out of the till. Think of the progress it could make if they tackled power shortages, invested in education and infrastructure, and improved farm yields!

One of the world's poorest countries, only twice the size of Ireland, Bangladesh already finds it hard to feed its people. According to the World Bank, nearly 56m out of a population of 147m are still poor. There will be 100m more mouths to feed by the middle of the century. Bangladesh is trading its only abundant resource, labour. Clothing exports, which account for 75% of total exports, more than doubled in the past five years to nearly $11 billion a year.

Over the same period, annual remittances by 5.5m Bangladeshis nearly tripled to $7.9 billion, or 10% of GDP, among the highest share in the world. So the economy is heavily dependent on spending in the high streets of Europe and America and on the demand for labour in the Gulf. Both are dropping off alarmingly (see chart). A closed capital account has protected the financial system. But Bangladesh's banks are far from robust. In February Fitch, a rating agency, called them among the weakest in emerging Asia.

A painful plunge
Bangladesh's:
% change on a year earlier, $ terms
remittances
exports
50
40
30
20
10
+
0
–
10
2003
04
05
06
07
08
Source: IMF

Domestic policymakers, who long denied the crisis would have a big impact in Bangladesh, now acknowledge that its pricing advantage over rival garment producers counts for little as demand in the West plummets. Yet no one knows how bad things will get. The IMF has said it is ready to assist, but the government has responded that it does not need help. The central bank insists that GDP will grow by around 6% this financial year (ending in June), compared with a 4.8% forecast from the World Bank last November.

Social unrest in Dhaka and Chittagong, the two big cities that account for about 60% of GDP, is already a real concern. This week, the government announced that it would sell rice at highly subsidised prices to millions of garment workers. But a fall in exports alone is unlikely to trigger a balance-of-payments crisis, since it will be accompanied by a big fall in imported inputs. Foreign-exchange reserves, hovering between $5 billion-$6 billion, are enough to cover two to three months of imports. And a sharp fall in food and oil prices has already considerably reduced the import bill. But remittances remain a worry. Last year 875,000 Bangladeshis took on jobs abroad. Saudi Arabia, the biggest employer, has hired only a few thousand workers since the start of the year. Airlines have already cut the number of flights ferrying workers to and from the Gulf.

Until the global financial crisis hit, Bangladesh was on track to meet the Millennium Development Goal of halving poverty by 2015. Progress on overall poverty reduction will depend on a number factors, including the birth rate. But "cash injections", either through microcredit loans or workers' remittances, have hitherto played a huge role. Alas, it might not be long before this changes.

Bangladesh's military

Mutiny in Bangladesh

Feb 26th 2009
From The Economist print edition

Reuters



Renegade troops cause havoc in Dhaka

ONLY two months after a return to democratic rule, Bangladesh's new government faces its toughest test yet. On February 25th the Bangladesh Rifles (BDR), a 45,000-strong paramilitary force, primarily responsible for guarding the country's borders, staged an armed mutiny. The renegade troops took 100 hostages and killed their commanding officer and many others. The army moved in to quell the mutiny. There ensued a 20-hour siege of the BDR's headquarters that left perhaps 50 people dead and turned a posh residential area of Dhaka into a battle-zone. Sheikh Hasina, the prime minister, offered an amnesty and in response the mutineers began to surrender. But the next day the rebellion rekindled and spread to a dozen other towns across the country. As *The Economist* went to press, there were reports that the army was taking control of BDR border posts and tanks were approaching BDR headquarters in Dhaka. The government has agreed to consider the mutineers' demands for better conditions. Another grievance is believed to be the BDR's exclusion from lucrative UN peacekeeping missions. The crisis will strain the army's relations with the new government, led by Sheikh Hasina's Awami League, which won a huge parliamentary majority in an election in December. Since then, Sheikh Hasina has moved swiftly to limit the army's role. However, with many of its officers among the dead, the army might resist the amnesty and push for the legal penalty for mutiny: death by hanging. And as ever in Bangladesh, with its long history of coups and counter-coups, there is speculation that such a rebellion would not be possible without the backing of a faction within the army itself.



WORLD ASIA

Tamil Nadu and Sri Lanka

Stoking the flames

Feb 26th 2009 | CHENNAI
From The Economist print edition

The politics of ethnic-Tamil solidarity and the Sri Lankan war

WITH kerosene and a box of matches, Sivaprakasam, a 60-year-old former civil servant, turned himself into a screaming fireball on February 21st. He was the fifth resident of Tamil Nadu, a southern Indian state that is home to 65m Tamils, to burn himself to death this year in protest at Sri Lanka's brutal campaign against its Tamil Tiger rebels. Tamil Nadu is known for self-immolation. Chennai, its capital, is dotted with monuments to seven "martyrs" who died in 1965, in a successful protest against the encroachment of Hindi on the Tamil language, deemed by its speakers India's oldest and richest.

The recent suicides will not save Sri Lanka's rebels, the Liberation Tigers of Tamil Eelam (LTTE), who for 25 years have fought for an Eelam, or homeland, for Sri Lanka's Tamils. Their embattled scrap of northern Sri Lanka is shrinking fast. Nor will the fiery protests in India do much for thousands of civilians held hostage by the LTTE. India's government, a coalition led by the Congress party, has quietly backed Sri Lanka's president, Mahinda Rajapaksa, in his two-year effort to wipe out the Tigers. One reason is personal: Congress's leader, Sonia Gandhi, lost her husband, Rajiv, a former prime minister, to an LTTE suicide-bomber in Tamil Nadu in 1991.

But some predict that anger in Tamil Nadu over events in Sri Lanka could affect the state-level outcome of a general election due by May. If recent history is a guide, this will in turn have a big influence on the make-up of India's next government. Tamil Nadu is certainly seething. Chennai's streets are pasted with posters of dead Sri Lankan women and children. In the villages, black flags hang from houses and daily protests are held. From his hospital bed, the state's invalid 84-year-old chief minister, M. Karunanidhi, has threatened to go on a hunger strike over the furore.

Mr Karunanidhi, a former screenwriter for the Tamil film industry who has led the Dravida Munnetra Kazhagam (DMK) party for four decades, is one of Congress's biggest coalition allies—and in a bind. Until Mr Gandhi's assassination, and a subsequent ban on the LTTE in India, he and every other political leader in Tamil Nadu openly supported the Tigers. Since then, only a few fringe parties have done so. Yet, as the violence in Sri Lanka roils local emotions, Mr Karunanidhi has felt obliged to demand an end to its government's campaign, which he has called "genocide". At the same time, he does not want to offend Congress, his most important ally.

Such tensions are normal in Tamil Nadu—and a sign of how flimsy its politicians' concern for their Sri Lankan cousins really is. In the state's increasingly fractured field, electoral alliances are more important than any issue—especially one that has not swayed an election for decades, if ever. The DMK sponsored the protest during which Mr Sivaprakasam lit his last match. Yet by championing the Sri Lankan cause, Mr Karunanidhi may in fact be most keen to deflect attention from nearer troubles. In one of India's more industrialised states, the economic slowdown is hurting, with thousands of jobs lost in textiles, computer services and car-making. Mr Karunanidhi's efforts to implant his relatives into government, including his son and anointed successor, M.K. Stalin, are also unpopular. In addition, the ailing leader no doubt hopes to outflank his main rival, a former film starlet and chief minister, J. Jayalalitha, who leads the All-India Anna Dravida Munnetra Kazhagam (AIDMK) party. A Brahmin in a mostly low-caste polity, Ms Jayalalitha is as nationalist as she is regionalist, and a fierce critic of the Tigers.

The danger for Mr Karunanidhi is that Congress might drop him for Ms Jayalalitha. A former ally of the Hindu-nationalist Bharatiya Janata Party, she is no friend to Mrs Gandhi. Yet, following the usual anti-incumbency logic, her prospects appear to be improving as the DMK's decline. She has urged Congress to withdraw its support for the DMK government in Tamil Nadu, and to consider forming a general-election alliance with the AIDMK.

Congress leaders in Tamil Nadu like the idea. But, for now, Mrs Gandhi does not. A Congress-AIDMK pact would risk uniting the pro-Tiger parties behind the rebels' sometime champion, the DMK. Perhaps only then could the Sri Lankan issue greatly shape the election's outcome. Moreover, Ms Jayalalitha is an

irascible ally, whom Congress, previously bitten, is twice shy of befriending—until after the election, that is, should she do especially well in it.

Pakistan's politics

Just like the bad old days

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From The Economist print edition

The two big mainstream parties are at each other's throats again

AP



"PAKISTANIS! Rise and revolt!" Thus thundered Nawaz Sharif, the popular opposition leader and former prime minister of Pakistan, after he was disqualified from holding public office by the Supreme Court on February 25th. The court also turfed his younger brother, Shahbaz Sharif, out of Punjab's provincial parliament and his post as its chief minister.

The court upheld a ban on the elder Sharif because he was convicted in 2000 of ordering the hijacking of a plane carrying the then army chief, General Pervez Musharraf, moments before his seizure of power the previous year. Under the constitution, convicts cannot contest elections. Therefore, having failed to launch an appeal against his conviction, as part of a deal he struck with Mr Musharraf at the time, to go into exile rather than languish in a Pakistani prison, Mr Sharif was disqualified.

His younger brother, Shahbaz, was also debarred by the court. So Punjab will now be run by its governor, Salman Taseer, until a coalition of the ruling People's Party of Pakistan (PPP) and the Pakistan Muslim League (Q), once Mr Musharraf's "king's party", proves it has a parliamentary majority there. Legally, the court's rulings against the Sharifs seem sound. But they are nakedly political, making them hugely unpopular, and may prove destabilising.

The case follows a falling-out between Mr Sharif and President Asif Zardari of the PPP (husband of the late Benazir Bhutto) who joined forces last year to oust Mr Musharraf, then the president. They also set up coalition governments in Islamabad, Pakistan's capital, and Punjab. Many doubted their two parties could ever work together, even in the national interest. So it proved. Defying Mr Zardari, Mr Sharif continued to insist on the reinstatement of Iftikhar Chaudhry, a deposed chief justice who has vowed to undo everything Mr Musharraf did, including his legal reprieve for Mr Zardari from corruption charges. Understandably, the president was against this. In an effort to circumvent his supposed ally, he therefore reinstated 56 other judges deposed by Mr Musharraf—but not their former leader, Mr Chaudhry.

Annoyed, Mr Sharif pulled out of the federal government several months ago. When the country's lawyers recently announced plans for a giant rally in support of Mr Chaudhry on March 12th, he vowed to support them. Unnerved by the prospect of his coalition partner in Punjab sponsoring an agitation against the PPP-led federal government, he encouraged the Supreme Court to rule against Mr Sharif.

Mr Sharif's response was blunt. "Zardari offered us a deal last month," he declared shortly after the court's ruling. "Ditch Iftikhar Chaudhry and support Hameed Dogar [the current chief justice, a Zardari favourite], and the court will absolve you." But, said Mr Sharif self-righteously, "we refused to budge on principles." He did not add the particular reason why he wants Mr Chaudhry back: to scrap changes Mr Musharraf made to the constitution, which at present forbid him from becoming prime minister for a third time.

Protests broke out across the main urban areas of Punjab following the judgment. Mr Sharif's Pakistan Muslim League (Nawaz) and other opposition parties are planning to band together with the protesting lawyers to raise hell. The press is also sympathetic to Mr Sharif. So in the short term, domestic Pakistani politics are going to get even uglier. That is the last thing America wants as President Barack Obama gets ready to unfurl a regional strategy for Afghanistan. At its core will be the necessity for a political consensus in Pakistan. No wonder Mr Sharif's first visitor after the court's decision was Bryan Hunt, the American consul-general in Lahore.

Somalia's civil war

Just a glimmer of hope

Feb 26th 2009 | NAIROBI
From The Economist print edition

After 18 years of strife, there is a small chance that a new Somali president and a new American one could make a fresh start

Getty Images



THE most smashed-up country in the world has reached a crossroads. The recent election of a moderate Islamist, Sharif Ahmed (pictured above), as Somalia's new president may offer the best chance of peace in the country for more than a decade. As head of the Islamic Courts Union that held sway over a chunk of Somalia in 2006, he was later driven into exile by invading Ethiopian troops backed by America. So it was quite a turnaround when, on his first day in office a few weeks ago, this courteous former geography teacher went to Ethiopia and got a standing ovation from heads of state in its capital, Addis Ababa, at an African Union (AU) jamboree.

This week he and his ministers went back to Mogadishu, Somalia's wrecked seaside capital. In his campaign he pledged to crush or co-opt Somalia's jihadists, who have taken over chunks of the country, and to rebuild national unity. Somalia has had no effective government since 1991, when a military dictator, Siad Barre, was toppled as the cold war ended. Could that change?

Mr Ahmed has a mammoth task. For a start, he has nothing resembling a proper government. His ministers are cobbled together from Islamists, secular nationalists, grizzled warlords and white-collar émigrés. They have no budget. He was elected by a parliament that can no longer meet in its own country. Its members operate at foreign donors' expense, staying in a plush hotel in the nearby country of Djibouti. A few weeks ago, Somali jihadists overran the dusty Somali town of Baidoa, parliament's official seat (see map below).

While the world has focused on a wave of piracy off Somalia's coast, which has threatened even the biggest ships heading for the Suez Canal or the Mozambique Channel, space has opened up onshore for jihadists that has not been seen since the Taliban gave Osama bin Laden his Afghan haven. Most of these fighters are loosely gathered around a group called the Shabab (Youth), which began as the armed wing of Mr Ahmed's Islamic Courts.

The original Shabab was shredded by Ethiopian artillery and American air strikes two years ago. The revitalised Shabab is sustained by a martyrdom complex. But its success is also due partly to money: it pays young Somalis to fight for it. It has also benefited from the decision of President George Bush's administration to isolate moderate Islamists such as Mr Ahmed and to embrace secular warlords with a history of terrorising civilians.



In the past few years, Shabab numbers have risen from a few hundred fighters to several thousand. The group controls the port towns of Kismayo and Marka, a number of places in the interior and parts of Mogadishu. It gets rake-offs from factories, warehouses, ports and airports, plus cash from Arab donors who see Somalia as a vital front in global *jihad*.

Local and foreign fighters, belonging to the Shabab or linked to them, are trained in camps beside Somalia's coastal mangrove swamps and in the scorching bush inland. They want to create a pure Islamist state, with hopes of acquiring the Somali-populated bits of eastern Ethiopia and north-east Kenya. The caliphate that emerged would be governed under a rigid Wahhabist interpretation of Islam, very different from the easy-going, mystical Sufism practised by most Somalis. The Shabab is ready to deploy suicide-bombers at home and abroad to further its cause.

Where it has control, it conveys its message with ruthless effect. When its people executed Abdirahman Ahmed by firing squad in the southern port of Kismayo in January, the event featured on al-Qaeda websites. What excited the viewers was the sight of an Islamist court, run by the Shabab and operating freely, publicly sentencing a 55-year-old politician to death. He had been found guilty of "showing sympathy for Christianity". His corpse was thrown into the infidels' cemetery to show he had worked with the occupying Ethiopian troops, whom the jihadists view as "crusaders", though many are Muslim.

Will the Shabab take over completely?

In the next few months, governments of countries with historical, humanitarian, commercial or strategic ties to Somalia, including its African neighbours, the United States, Italy, Britain, Sweden, Saudi Arabia and the Gulf states, must decide whether to spend time and money to give Mr Ahmed a chance to rescue his benighted country. If they do not, he will very probably fail—and the country with him.

The battleground is Somalia's centre and south, which has water and food. Everywhere the complex mix of clans and sub-clans is combustible. By contrast, the arid north, peopled largely by nomadic camel-herders, is fairly peaceful. Puntland, in the north-east, is semi-autonomous, but most of its people want to be part of a federal Somalia. It hosts some of the pirates, as well as people-traffickers, kidnappers and a fair number of jihadists. But its government has disarmed freewheeling militias and more or less keeps order.

The recently ousted previous Somali president, Abdullahi Yusuf, a Puntland warlord, has taken several hundred gunmen back north from Mogadishu and now seems more interested in his businesses, mainly in the town of Bossaso. Somaliland, a former British territory, has been fairly stable since it declared independence in 1991. If coming elections there go well, with voters using biometric identity cards, it may slowly start to win recognition from some African countries and others farther afield. It is not clear what Mr Ahmed thinks about independence for Somaliland. But nationalists and jihadists are violently against it, as is Puntland, which disputes a border zone with it.

What is clear is that no one controls the country, neither the government, nor the Shabab. But, certainly until Mr Ahmed's arrival, the Shabab have been in the ascendant. Its system of 20 to 30 men per cell, each one locking into larger command structures when they take a town, is hard to crack. Hardened by battle, hunger and disease (often malaria), the Shabab fighters are difficult for foreign security services to track. They pass easily between Somalia and Kenya and from there into Somali communities in Europe and America. Foreign intelligence services think a Shabab terror attack sooner or later in Nairobi is likely. Some airlines may soon stop flying to Nairobi's Jomo Kenyatta Airport because of threats.

London and other Western cities could well become targets too. The FBI apparently put the Shabab high on its list of outfits that might have tried to launch an attack during Barack Obama's inauguration. A suicide-bomber, Shirwa Ahmed, who blew himself up in a Shabab operation in northern Somalia in October, was an American citizen, one of 100,000-odd ethnic Somalis resident in Minnesota.

So what's the cure?

Nearly all Ethiopia's occupying troops have now withdrawn from Somalia. Since then, the Shabab has begun to use suicide-bombers and roadside bombs in an effort to drive out the 3,400-odd remaining AU peacekeepers, who guard a few streets around the port, airport and presidential palace. Last week 11 Burundian peacekeepers were killed by Shabab suicide-bombers. Earlier in February a remote-controlled landmine wounded several of them. In a panicky response, the AU soldiers opened fire, killing at least 20 civilians—just what the Shabab wanted.

Whether or not foreigners have been involved, peacemaking has failed for the past 18 years. Since Mr Barre fell, no fewer than 16 concerted efforts to make peace have foundered. Mr Ahmed may fail too. Many people profit from the long war and want to keep it going. Some siphon off aid money, others move heroin through Mogadishu or traffick people by sea to Yemen. Somali pirates are often sponsored by Somali businessmen abroad.

Many Somalia-watchers think Somalis should work out their own political settlement—and that foreigners should keep out. Somehow the Shabab has to be crushed, perhaps bringing some of its more amenable members into Mr Ahmed's apparently moderate Islamist fold. The Shabab may not be as cohesive as it claims to be. The recent departure of the hated Ethiopians and the Shabab's own record of bullying the impious and smashing the gravestones of Sufi saints have lost it some support. Its two top commanders, Muqtar Robow and Hassan Turki, may become isolated if Mr Ahmed's government holds up, especially as many of the Shabab fighters come from the new president's own Hawiye clan. Thanks to some back-channel talks, some Shabab, including an influential commander in the town of Jowhar, have already changed sides.

Crush them or co-opt them

Plainly the Shabab will be hard to deal with, whether by force, negotiation or trickery. With its training camps, arms caches and money, it is more than just an Islamist outgrowth of Somalia's intricate clan politics, which has generally determined the balance of power in the country. Aden Hashi Ayro, a Shabab commander killed by an American missile last year, still has a following, even in death. If foreigners keep out and the AU withdraws the remnants of its peacekeepers, the Shabab may simply fill the vacuum, tighten its grip on the south and exert more power nationwide by controlling the supply of food to a hungry people. Civil strife could turn into sectarian war, with secular warlords presenting themselves as Sufi sheikhs in the fight against the Shabab.

AP



The boys in black who want the new man to fail

Alternatively, if Mr Ahmed is too indulgent as he seeks to buy off the Shabab, Somalia may get a

caliphate by stealth. If, however, he keeps on good terms with Ethiopia and America and refuses to institute *sharia* law, as he promises, he may lose support in Mogadishu, where an influential group of clerics has called for *sharia*'s imposition, including public executions.

Some suggest, as a first step, that Mr Ahmed should persuade the International Criminal Court (ICC) at The Hague to indict Somalia's worst offenders. Human-rights campaigners wonder why thugs are being brought to justice in Liberia, Sierra Leone and even, most recently, in Congo, but have never been indicted for crimes in Somalia. They fear that the latest peace effort may strengthen a culture of impunity by letting warlords off scot-free as a reward for coming on board. Proponents of using the ICC say that Mr Yusuf, the last president, was forced to step down partly because of threats that he would face an international travel ban and an assets freeze if he clung to office.

Another proposal is to set up an international "green zone" in Mogadishu. But in present circumstances, there is no chance of Western armies establishing themselves in the lawless capital. Nor are United Nations peacekeepers likely to hunker down there. Some suggest extending the mandate of the AU's present embattled force of Ugandans and Burundians for another year. The AU troops could perhaps be bolstered by private security firms to let UN offices and foreign embassies be re-established in Somalia, helping Mr Ahmed get a grip on Mogadishu. At the least, the airport should be secured. The UN's special envoy, Ahmedou Ould-Abdallah, a former foreign minister of Mauritania, says he is determined to move his office from Nairobi. "Why [is there a green zone] in Baghdad and Kabul but not in Mogadishu?", he asks plaintively. But previous efforts to bring in effective peacekeepers, whether African or UN, have all failed.

In any event, Mr Ahmed's government needs cash—to pay for basic services and to reinforce his own fledgling security force. For instance, the UN has trained 3,000 Somali police, but they have not been paid for a year. Somali businessmen say outsiders—Saudis are most often mentioned—could bankroll the new government and do more to spur free enterprise by buying livestock and investing in fishing.

If the UN and Western governments remain loth to get involved, Mr Ahmed will hope for more energetic regional diplomacy. Ethiopia and Eritrea, bitter rivals, have used Somalia as a battlefield for a proxy war. Ethiopia has kept its promise to Somalia's more moderate Islamists that it would remove its troops and has publicly backed Mr Ahmed. His fragile government would be helped if Eritrea's was persuaded to cut its links with the radical Somali Islamists it has been backing merely to hurt Ethiopia. But according to some reports, Eritrea has recently flown several planeloads of arms into Kismayo to bolster the Shabab. It may also help Iranian and Arab sympathisers to send arms and explosives.

Though unlikely to get deeply involved, Barack Obama's administration may have a chance to help too. It is likely to continue to foster cosy relations with Ethiopia, despite that country's poor human-rights record, and may want to be tougher with Eritrea. Backing Mr Ahmed, at least with cash and diplomatic support, would meet part of Mr Obama's inaugural promise to put out the hand of friendship to those who unclench their fist. But it seems likely, at any rate at first, that Mr Ahmed will be on his own, while al-Qaeda and its friends continue to view ungoverned Somalia as a promising territory for infiltration.

Somalia's demography

Little-known, dispersed and dying

Feb 26th 2009 | NAIROBI
From The Economist print edition

No wonder no one knows for certain what should be done

HOW many people still live in Somalia? No one knows. The UN says around 10m. Just as Somalia's problems of jihadism and piracy have gone global, so have its people. War has scattered Somalis across the world. But the diaspora is probably at least 1m-strong—favourite outposts include Cardiff, Dubai, Minneapolis and Stockholm—and plays a big part in the country's politics. These figures exclude the 6m-plus ethnic Somalis who live in neighbouring Ethiopia, Kenya, Djibouti and Yemen. Many MPs carry foreign passports. Remittances from abroad are all that keep the economy afloat.

"We know less about [the country] today than at any time in the last 100 years," says Ken Menkhaus of Davidson College in North Carolina. One reason is that it is too dangerous to visit. Many diplomats working on Somalia have never been there. Some experts have not been for years. The UN's special envoy, Ahmedou Ould-Abdallah, thinks some of the specialists on the country, who are often paid handsomely by international bodies and government agencies, are part of the problem. "The Somali peace agenda has been held hostage by so-called experts," he says.

Dozens of aid workers, campaigners and journalists, most of them locals, have been killed in the past year or so. Hundreds more have been beaten, threatened or forced into exile. Many, including two freelance journalists from Australia and Canada, are still held hostage. Just as this correspondent was about to visit southern Somalia with people from the UN's World Food Programme, the trip was cancelled when two of the agency's workers were shot dead and a third died on an airstrip waiting for medical help. Intrepid charities such as Médecins Sans Frontières and the International Committee for the Red Cross rarely send in foreign staff. Businessmen in Mogadishu say they can no longer trust their hired gunmen to protect foreigners. Most analyses of Somalia, including this one, are written in Kenya, based on second-hand reports.

But one thing is indisputable: Somalia is one of the world's most pressing humanitarian emergencies. With famine looming, food prices high and the local currency going down, the situation is worsening. Emergency feeding stations for children are packed. Some 3.2m Somalis now depend on food aid, at least two-thirds more than in 2007. Aid is shipped from the Kenyan port of Mombasa with a foreign naval escort to protect it from pirates. Less than a quarter of Somalia's children go to school; Somalia may soon be Africa's most illiterate country. Its maternal mortality rate may be the highest in the world.

Since the Ethiopians invaded at the end of 2006, at least 10,000 Somalis have been killed in fighting and more than 1m displaced. Despite a UN arms embargo, small arms still flow in. The newest AK-47s in Mogadishu's Bakara market were made in Libya in 2006. It is reckoned there is almost one gun for every man, woman and child in the city.

Bishop's move

Feb 26th 2009 | JOHANNESBURG
From The Economist print edition

Will a new opposition candidate for the presidency dent the ruling party?

AP



President Dandala?

WITH just two months to go before South Africa's general election, the Congress of the People (COPE), a splinter of the ruling African National Congress (ANC), has presented a political unknown, Bishop Mvume Dandala, as its presidential candidate in a bid to attract votes.

Since its launch late last year, COPE has been struggling to distinguish itself from the 97-year-old liberation party of which its founders were so recently an integral part. With Bishop Dandala, a former head of the Methodist Church of Southern Africa and of South Africa's Council of Churches, it hopes to present a squeaky-clean image in contrast to the sleaze that is plaguing the ruling party and its own presidential candidate, Jacob Zuma.

Some have hailed the move as a master stroke, providing the prospect of the first real challenge to the dominant party since South Africa became a democracy in 1994. The country's interim president, Kgalema Motlanthe, a deputy president of the ANC, said the bishop's candidacy would add "oomph" to the electoral contest.

But others are less impressed. However fine the moral and intellectual credentials of the 57-year-old bishop, who has a master's degree in theology from Cambridge University and two doctorates in theology and philosophy, he has scant political experience and is little known among South Africa's poor blacks, who cast the bulk of the vote. Sceptics suspect his candidacy is part of an effort to disguise a power struggle between COPE's leader, Mosiuoa "Terror" Lekota, and his deputy, Sam Shilowa.

Most pundits reckon that COPE is backed by about 10% of the voters. The only other serious opposition party, the Democratic Alliance, led by Cape Town's forceful mayor, Helen Zille, may again get the 12% or so of the votes it polled in the last general election in 2004, but it is still handicapped by its predominantly white middle-class image; COPE, though also widely seen as too middle-class, is drawing support from across the racial divide. So the guess is that the ANC will still get a good two-thirds of the vote in the coming election, on April 22nd. The new parliament then chooses a president. It is in the longer run that COPE may have the potential to break the ANC's stranglehold on power.

For the ANC seems to be sinking deeper into a mire of corruption. The ebullient Mr Zuma, soon (it is said) to marry his sixth wife, is struggling to fend off a string of charges against him for corruption and tax evasion. A trial has been set for August, when he will very probably be South Africa's head of state. Last week Carl Niehaus, the ANC's spin doctor and a former ambassador to the Netherlands, resigned after admitting to a web of lies, fraud and debt that financed a lavish lifestyle and must have been obvious to his bosses.

The South African Institute of Race Relations, a think-tank, has given warning that the spreading allegations of fraud and corruption in the ruling party may come to compromise the country's rule of law. "It appears as if certain political leaders take the presumption of innocence to mean that they can remain in office while under suspicion, regardless of the damage that does to their political party or to government," says the institute's deputy director.

Meanwhile Ipsos Markinor, a market-research firm, has published a poll taken in November, before the global economic storms had fully affected South Africa. It suggests that, for the first time since the onset of democracy, more South Africans feel their country is moving in the wrong direction (42%) than in the right one (38%).

Senegal

Trouble at home

Feb 26th 2009 | DAKAR
From The Economist print edition

President Abdoulaye Wade will ignore domestic discontent at his peril

ONCE a source of delays and frustration, the drive from the airport into downtown Dakar is now quite a joy. Four lanes of tarred road sweep past gleaming mansions near the airport and hug the palm-fringed Atlantic beachfront right into the town centre. La Corniche, as it is known, is one of President Abdoulaye Wade's "great projects". He trumpets it as a symbol of his achievements. But to his critics it is a source of ammunition for allegations of corruption, nepotism and the president's allegedly growing lust for power.

Long hailed as a beacon of democracy in a corner of Africa plagued by conflicts and chaos, Senegal is going through its own hard times. Mr Wade is facing unprecedented rage and frustration. Since he took office in 2000, after 22 years as the country's main opposition leader, a growing number of his people are disappointed.

Yet the country had been doing rather well. Its relatively good communications network had brought investment into businesses such as call centres, challenging Francophone north African countries as outsourcing destinations for France. Senegal has also profited from recent years of chaos in nearby Côte d'Ivoire, once Francophone west Africa's financial hub; many international organisations and banks have switched to Dakar from Abidjan, the Ivorian commercial capital, bringing rich expatriates and a building boom.

Arab countries too have invested a lot in Senegal. The Organisation of the Islamic Conference (OIC) held its summit there a year ago after several delays in finishing the preparations, including the Corniche. Mr Wade likes to be seen as a continental statesman. He has tried to broker talks to end crises in Zimbabwe, Sudan's Darfur region and Chad. To display his lofty ambitions, another project, a huge statue symbolising "Africa's Renaissance", overlooking Dakar, is being built by North Koreans.

But close to home, many Senegalese are less impressed. "These meetings, these roads and these houses," grumbles a Dakar driver. "The politicians are corrupt and we're still poor." The country has not escaped the impact of soaring commodity prices. The normally easy-going capital has had its share of demonstrators calling for measures to tackle the food crisis instead of building glamorous projects.

Some of Mr Wade's friends fear he has dynastic ambitions. Re-elected in 2007, he has plenty more time in office. But many Senegalese think he is lining up his son, Karim, to succeed him. The younger Mr Wade ran the OIC summit. In its aftermath, several grand hotels were left unfinished. When parliament's speaker, a member of the president's party, too noisily called for an inquiry, he was sacked.

So Senegal's democratic credentials are being questioned. Rows between the government and the press have become frequent. A prominent newspaper publisher, El Malick Seck, was jailed for printing a controversial article about the president and his son. And democracy-minded Africans elsewhere were disappointed when Mr Wade seemed to endorse a military coup late last year in neighbouring Guinea after the death of its long-time president.

Shias in the Gulf

Grumbling and rumbling

Feb 26th 2009 | CAIRO
From The Economist print edition

Shia unhappiness is rattling regimes in Saudi Arabia and elsewhere in the Gulf

EPA



Women versus women in Bahrain

LIKE the crude oil that lies in vast pools beneath the Persian Gulf, tensions between the region's Sunni and Shia Muslims tend to stay below ground. But when pressures build and a ready channel is cleared, they can bubble to the surface with alarming force. Thirty years ago the Islamic revolution in Shia-majority Iran inspired a wave of unrest among fellow Shias of the opposite shore. Things then calmed down. Nervous Arab rulers, all of them Sunnis, soothed their Shia subjects with a few rights and promises of more, while Iran largely gave up trying to export its revolutionary fervour.

But with Iran lately sounding more aggressive under President Mahmoud Ahmadinejad, small incidents are again triggering bigger eruptions. On February 20th, for instance, a group of female pilgrims visiting the most revered Shia site in Saudi Arabia, a cemetery in Islam's second-holiest city, Medina, where hundreds of the Prophet Muhammad's descendants are said to have been buried, screamed when they spotted what they guessed was a religious policeman filming them from on top of a security wall. Male relatives, outraged by this invasion of modesty, demanded the footage. Instead, the all-Sunni police force arrested five of them, sparking a riot by thousands of Shia pilgrims, more arrests and injuries. Repeated protests over several days then spread from Medina to Saudi Arabia's Eastern Province. That province contains many of the kingdom's Shia minority, numbering about 10% of Saudis, as well as most of its oil reserves.

As Shia clerics weighed in with calls for an end to what they called systematic persecution, Sunni extremists accused the *rafida*, an abusive term for Shias, meaning rejectionists, of acting as a fifth column for Iran. “Today they besiege the religious police,” howled one website commentator. “Tomorrow they will encircle the Eastern Province along with the Shias of Bahrain and with Iranian backing.” The Saudi king should “strike them with an iron fist”, declared the writer. Another suggested that the Shias be hurled into the Red Sea or, better still, dropped onto the Iranian shrine city of Qom.

Mention of Bahrain carries particular resonance. It was in this tiny neighbouring island kingdom, where two-thirds of the citizens are Shias and where the American Fifth Fleet is based, that sectarian troubles loomed alarmingly in the 1980s. More recently, in December, Bahrain's authorities accused 35 Shias of plotting to overthrow the state. Since then, sporadic riots have rocked the poor Shia villages that ring Bahrain's capital, Manama. In January three human-rights campaigners were arrested. This week 21 people, including two of the human-rights activists, appeared in court, accused of planning to ambush policemen and bomb public property, shopping malls, markets and hotels.

Yet when Iranian politicians recently sniffed that Bahrain used to be an Iranian province, Bahrain's main Shia parties were quick to reaffirm their Arab identity, joining a chorus of Arab protest that led some commentators to remark pointedly that several Iranian provinces happen to house large Arab and Sunni populations. Fearing damage to the reputation it has tried to build as a defender of pan-Islamic causes, Iran hastily apologised to Bahrain.

The ugly nearby example of sectarian strife in Iraq, though it has subsided in the past two years, has left little appetite in the region for more trouble of that kind. Despite suspicions of their loyalty, Shia Arabs tend to look not to Iran but to their own spiritual leaders for guidance. Yet with Iran determined to chase the Arabs' American ally from the Gulf, and with Shia Arabs often still suffering political exclusion and social stigma, unrest is likely to break out from time to time. Considering local, regional and international variables, a clash between the Saudi regime and its Shia citizens is a matter of time, reads an ominous analysis on a popular Saudi website.

Israel's would-be government

The right has the first shot

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From The Economist print edition

Many variations are possible, but the right is first to try to form a government

BINYAMIN NETANYAHU, Israel's prime minister-designate, has begun negotiating with his Likud party's "natural allies" for a right-wing-cum-religious coalition government. Still, though at first rebuffed, he has not quite given up hope of luring both Tzipi Livni, the leader of the centrist Kadima party, and Ehud Barak, her Labour counterpart, into a unity government of a milder complexion. He has until April 2nd to find a majority in the 120-seat Knesset. Various permutations are still being aired.

Ms Livni, foreign minister in the outgoing Kadima-led government, says she will not provide a fig-leaf for the harsher policies she believes would hurt the country. She says that when she and Mr Netanyahu met on February 22nd he would not even acknowledge the need for a two-state solution for Israel and Palestine, let alone seriously discuss a common policy for trying to bring it about. Mr Netanyahu offered parity in the cabinet between Likud, which won 27 seats to Kadima's 28 in the general election on February 10th, but Ms Livni complains that her party would then be permanently outnumbered by the Likud-led block. Mr Barak says simply that having done so badly in the election, with only 13 seats, Labour needs to spend the next term in opposition, rebuilding itself.

The haggling and the refusal so far by both leaders of the two strongest parties to back down have rekindled a debate over whether Mr Netanyahu, who was prime minister from 1996 to 1999, is ultimately a pragmatist or at heart still an ideologue of the old school. Those who say he is a pragmatist point to the agreements he signed with the Palestinians in his first term and to the secret negotiations he held with Syria. Those who say he is an ideologue, wedded to the idea of a Greater Israel that would take in the West Bank and stretch down to the Jordan river, recall his niggardly foot-dragging during those negotiations.

Mr Netanyahu now says that Palestinian statehood is not possible in the foreseeable future. The Palestinian Authority on the West Bank is weak and ineffectual, and he could not negotiate with the Islamists of Hamas as they are terrorists who must be toppled from power. In the election campaign he rejected sharing Jerusalem with the Palestinians and said he would not withdraw from the Golan Heights, a slice of Syria that Israel has held since 1967.

Even with such hard views, putting together a coalition of like-minded allies will not be easy. There are tensions between the far-right secularists of Yisrael Beitenu, which has 15 seats, and other more religious-minded groups over a proposal to bring in civil marriage and loosen the rabbis' grip on matters of personal status. Yisrael Beitenu also wants drastic reform of the electoral system, as do many in Likud and on the left. But such proposals could spell the demise of the small religious parties whose votes Mr Netanyahu needs to secure a majority. Or they might be forced to merge with each other, a prospect they think only slightly less ghastly.

Allocating top jobs will also be tricky. Yisrael Beitenu's leader, Avigdor Lieberman, who campaigned on an anti-Arab platform, wants a juicy plum. His 15 seats make it hard for Mr Netanyahu not to give him one. Mr Lieberman's first choice is the Defence Ministry, but Mr Netanyahu may prefer to hand it to Dan Meridor, a Likud minister who veered left in 1999 to join a short-lived Centre Party and has veered back to the right again. Mr Lieberman may settle for the Finance Ministry; but the police are investigating him for alleged money-laundering, so that may be awkward.

He might end up as foreign minister, a prospect which, in view of his history of undiplomatic remarks, has raised eyebrows, to say the least. Last year he said Egypt's President Hosni Mubarak should "go to hell" for refusing to visit Israel. "Foreign ministers aren't used to my style," he has conceded. "But don't worry, everyone will welcome me, including Egypt."

Germany

Europe's reluctant paymaster

Feb 26th 2009 | BERLIN
From The Economist print edition

AP



The German government may have to concede, through gritted teeth, that it cannot avoid helping financially strapped governments in Europe

ITS place on the map once worried its generals. Now Germany feels encircled by economic menace. To the east lie ex-communist economies suffering from tumbling currencies and a drying-up of foreign capital. To the south and west are countries that are in the euro but have kept their profligate ways. Their cost of borrowing has shot up, stirring fears of default. Some now talk of a possible break-up of the euro area.

At times like these people turn to Germany, the biggest and most creditworthy economy in Europe. Austria, where the banks have risked more than most in eastern Europe, wants the European Union to provide €150 billion ($191 billion) of aid, part of it to countries that are not even members of the EU. Robert Zoellick, president of the World Bank, thinks east European banks need €120 billion of fresh capital, much of which may have to come from western Europe. The clamour for assistance to weaker countries in the euro is almost as loud.

For Germany, this poses a dilemma. It championed both the single currency and the EU's eastward enlargement and now sends most of its exports to countries that are in the EU. But such partnerships bring the risk of instability, and Germany has long insisted on safeguards against infection. East Europeans are welcome to buy goods from Germany but not freely to find jobs there. At German insistence, countries in the euro must tame their public finances and cannot be bailed out.

The credit crunch makes it harder for Germany to practise this form of economic safe sex. In October the finance minister, Peer Steinbrück, brusquely rejected a French-backed plan for a common fund to rescue banks, fearing that Germans would pay for the mistakes of bankers in other countries. Loth to give up its goal of balancing the budget by 2011, Germany was at first reluctant to adopt a fiscal stimulus. Now it is being asked to help partners that did less to control debt or adapt to the euro's discipline. Otmar Issing, a former chief economist of the European Central Bank, spoke for many when he said that making euro members pick up others' debts "would take an axe to the stability of the currency union". Such admonitions can frighten voters, an especially pertinent concern seven months before an election.

Yet Germany may in reality have little choice. On February 16th Mr Steinbrück admitted that some countries in the euro, especially Ireland, were in trouble. If one were in danger of defaulting, he said, "the collective would have to help." These comments were interpreted as a signal that Germany would agree to circumvent the no-bail-out rules. *Der Spiegel*, a magazine, claimed that the Finance Ministry was

contemplating several alternatives, including aid from the EU (with tough conditions attached) and a "common bond" that would exploit the financial strength of the most creditworthy to assist the weakest.

Mr Steinbrück was misinterpreted, said his ministry. Countries in difficulty should adopt the "normal policy mix" of reducing budget deficits and improving their competitiveness. Assistance, if required, would be decided case by case; in any event, no country was in immediate danger. Mr Steinbrück's ambiguity may have been deliberate. The mere hint that aid might be available caused the financing costs of weaker countries in the euro to fall.

If conditions worsen, discussion may shift from whether to bail out countries to how. It may paradoxically be easier to help east Europeans than those bound by the euro's no-bail-out rules. The EU, with the IMF and World Bank, has given support to Hungary and Latvia. In November it raised the ceiling for balance-of-payment loans to non-euro countries to €25 billion.

But the idea of a common bond to help weaker countries, which would raise the financing costs of stronger ones, may be a non-starter. "If you want to stir anti-European sentiment, a European bond is the way to go," says Sebastian Dullien, an economist at the University of Applied Sciences in Berlin. Hans Eichel, a former finance minister, suggests instead a lending facility with IMF-style conditions run by the European Commission.

Indeed, bail-outs may be a roundabout means to get the stability Germany craves. Borrowers would have to improve their finances and competitiveness. EU countries, in and outside the euro, would have more reason to co-ordinate economic policies (which for Germany might mean relying less on exports and more on domestic demand). Borrowers outside the EU might inch closer to membership. Europe could "use this crisis to strengthen integration", says Mr Eichel. Perhaps, but only with Germany's help.



WORLD
EUROPE

Protests in France

Allons, enfants!

Feb 26th 2009 | PARIS
From The Economist print edition

French fears that protests will spread from the Caribbean to the mainland

THERE was a time when Nicolas Sarkozy relished crisis management. His fearless, no-nonsense approach resolved more than one stand-off. Few people have forgotten how, as a young mayor of Neuilly 16 years ago, he walked into a nursery school and negotiated with an armed hostage-taker threatening to blow up the building. Yet a series of protests, overseas and on the mainland, are now testing the president's skills to the limit.

The most turbulent have been on the island of Guadeloupe, a French department in the Caribbean that has been paralysed by a general strike. One union member was shot dead when matters turned violent. Although the island seems calmer now, the strike goes on, as does the conflict between the government and the unions, which want a €200 ($256) monthly pay rise. This week trouble broke out in Martinique, a neighbouring island, with cars burned and shops looted.

The biggest fear is that the turmoil may spread to the mainland. In recent weeks, high-school pupils, teachers, university researchers, railwaymen and car workers have taken to the streets. On one day in January some 1m-2.5m people protested against low pay and job cuts. Unions have called another day of action for March 19th. In a poll, 63% of respondents said the violence in Guadeloupe could spread to mainland France.

In many ways, the troubles in Guadeloupe and Martinique are specific. With their French post offices, town halls, prefects and use of the euro, they are in theory French administrative departments. In reality, the state pumps €13 billion a year into the overseas territories in subsidies and tax breaks, including a 40% salary premium for civil servants. Yet unemployment is three times as high as on the mainland, and GDP per person just over half as big. Prices of goods such as yogurt or fresh beef are on average 34% higher, according to *France-Antilles*, a newspaper.

A demand for higher pay to compensate set off the strikes in Guadeloupe. Mr Sarkozy's government is in talks with the unions. Yet the protests are racial as much as economic on an island where the white minority owns most businesses. The main protest group calls itself, in creole, Movement against Pwofitayson, a blend of the words "profiteering" and "exploitation". Elie Domota, its leader, who is a securely paid French civil servant, talks of re-establishing "the legitimate rights of blacks as the majority people". The struggle is an unusually toxic mix of neocolonial resentment and economic unrest.

There are still grounds for worrying about contagion. French opposition politicians have piled in to Guadeloupe to "express solidarity", implicitly linking the struggle to home. The poster-boys of anti-capitalism have made the trip, including José Bové, a sheep-farmer-turned-campaigner, and Olivier Besancenot, a hard-left Trotskyite leader. Even Ségolène Royal, a Socialist former presidential candidate, dropped in this week, proclaiming, "Let's remember the French Revolution!"

Many anxieties in Guadeloupe exist in France too. After meeting union leaders recently, Mr Sarkozy tried to head off more conflict by offering to raise family allowances, reduce income tax for the lowest-paid and boost unemployment insurance. But the unions also want a higher minimum wage, a cut in VAT and an end to civil-service job cuts. Union elections to company works councils are due in March, and nobody is in the mood to compromise.

One person who spoke to the president recently says he is "extremely tense". He needs to make sure that public opinion does not swing behind the strikers. Yet ordinary people feel they are paying for the excesses of others, so many support the protesters. Paradoxically, they may do so even more because of new rules guaranteeing minimum service, ensuring that strikes do not paralyse public transport.

Mr Sarkozy needs to tread a line between helping the most vulnerable and resisting demands that would weigh on the public purse in the long run. But his popularity has sunk by seven points, to 37%. He has

not helped himself by publicly ridiculing professionals, such as university lecturers, whom he is trying to encourage to accept reform. Above all, his action-man style leaves him exposed. By taking most matters into his own hands, in contrast to the patrician aloofness of his predecessors, he has robbed himself of one trick many of them used: blaming the prime minister when things go wrong.

Protests in Ireland

In a stew

Feb 26th 2009 | DUBLIN
From The Economist print edition

Tough times for Ireland's government—and its people



No apostrophe either

WHEN more than 100,000 people paraded through Dublin on February 21st, it was the biggest march the Irish capital had seen since 1980. Then, binmen joined bankers in protest against Ireland's high tax rates. This time there was less social solidarity. The marchers were mostly public-sector workers angry over a plan to cut their pay, via a 7% pension levy. They were also outraged by the behaviour of bankers, whom one union leader accused of economic treason.

The government has injected €3.5 billion ($4.5 billion) into each of the country's two largest banks, but this has not impressed markets. Shares in Allied Irish Banks and Bank of Ireland have fallen sharply. After the bursting of the property bubble, more than €7 billion may be needed to cover bad loans to developers. In January the government nationalised Anglo Irish Bank (often seen as the builders' bank), after its chairman, Sean Fitzpatrick, failed to disclose some €83m in personal loans. This week anti-fraud police raided the bank to investigate alleged breaches of company law.

The prime minister, Brian Cowen, faces two crunches: the banks and the public finances. So far, he has had little success in tackling either. His government's popularity ratings, and his own, have dived. He is struggling to avoid nationalising the two biggest banks. And his fiscal plan is in trouble. It aims to keep the budget deficit below 10% of GDP this year (the highest in the European Union), and to achieve balance by 2013, via spending cuts and tax rises worth 8% of GDP. Tough, yet most economists doubt it is enough. The European Commission is sceptical. The government's proposals, it has said, lack detail and its growth assumptions are too optimistic.

This may force the government to try to trim the deficit sooner, this year and next, not later in its five-year plan. That would mean raising taxes earlier than expected. Mr Cowen had been hoping to delay that unpalatable medicine. He faces European and local elections in June and, in the autumn, a second referendum on the EU's Lisbon treaty, which recent polls suggest should be winnable. The state now pays higher rates on its bonds than Greece. With increasing talk of potential default on its sovereign debt, Ireland has become the weakest link in the euro. Mr Cowen has little time left to turn things round.

A spy scandal in Estonia

How many more?

Feb 26th 2009 | TALLINN
From The Economist print edition

A senior Russian spy in NATO is convicted

WHY he did it is still unclear. But the “how” is leaking out. Hermann Simm, a former Estonian official who was one of Russia’s highest-placed spies in NATO, pleaded guilty to treason on February 25th and was jailed for 12½ years. The Estonian authorities have released some details of a case that has had the spook world buzzing for the past year.

Russia’s foreign intelligence service, the SVR, recruited Mr Simm on his holiday in Tunisia in 1995. He was a prime catch. He had finished a stint as a top policeman, and was starting a new security job at the defence ministry. The approach was made by Valery Zentsov, once a KGB officer in Soviet-occupied Estonia. Mr Simm was neither blackmailed nor, at first, bribed; he just wanted his Soviet-era rank of colonel back. At a third meeting he was put on the payroll, receiving just over $100,000 in all.



Zentsov, the man who hooked Simm

Mr Simm betrayed every secret that crossed his desk. There were plenty: as the man in charge of Estonia’s national security system, he organised the flow of all classified military documents in the country and abroad. Once Estonia joined NATO in 2004, he acted as the Kremlin’s eyes and ears on the alliance too (although his poor English, say some, may have limited his usefulness). He also tried but failed to get hold of secrets from Estonia’s security and intelligence services, which are separate from the defence ministry.

In 2002, say Estonian officials, Mr Zentsov was replaced by another Russian handler. Sergei Yakovlev worked for the SVR’s elite S-directorate, which runs “illegals”: spies who acquire a genuine identity in a foreign country. Mr Yakovlev, a near-native speaker of Portuguese, appears to have acquired Portuguese citizenship illegally, gaining a passport in the name of Antonio de Jesus Amurett Graf. Travelling as a business consultant, he met Mr Simm every three months or so, in at least 15 countries in the EU and elsewhere.

The plan came unstuck because of poor spycraft. According to spycatchers elsewhere, Mr “Graf” tried to recruit a senior official in another country, who reported the incident to his own counter-intelligence service. Under scrutiny, the Portuguese was seen meeting Mr Simm. That set alarm bells clanging across NATO. The difficulty was to observe Mr Simm closely enough to build a criminal case without sparking his suspicion. Estonia’s security service is getting many plaudits for this, which culminated in his arrest last September. In a separate prosecution, Mr Simm was ordered to pay 20m Estonian kroons ($1.7m) for the cost of new security systems. The SVR did not immediately reply to a request for comment.

Mr Simm is not the only Russian spy at high level in NATO. Several other countries are apparently following up five leads arising out of Mr “Graf’s” activities. The results are unlikely to become public. The way in which Estonia put Mr Simm openly on trial is striking. In other countries, those caught spying for Russia tend to be eased out discreetly rather than being brought to justice in the painful light of day.

Albanian politics

Time for a change?

Feb 26th 2009 | TIRANA
From The Economist print edition

The forthcoming election looks like being a close contest

THE general election is four months off, but it feels closer. Every day Albania's politicians are on the stump, addressing packed town halls and assembling campaign teams. Edi Rama, the colourful leader of the opposition Socialists, is underlining phrases in a book of Barack Obama's speeches. For change will be Mr Rama's mantra as he challenges Sali Berisha, prime minister and leader of the Democratic Party. Mr Berisha has been at the heart of Albanian politics since the collapse of communism in 1991. Those born that year will be voting for the first time. They have no memory of communism, but also none of a time before Mr Berisha. Mr Rama thinks this is to his advantage.

Yet Mr Rama is not quite a new figure on the political landscape. The 44-year-old has been mayor of Tirana since 2000. He has transformed the city. Illegal buildings that scarred its centre have been bulldozed, grey blocks painted in colourful designs and plans are afoot to transform Skanderbeg Square into a pedestrian zone. Tirana is no longer the chaotic, declining city of the 1990s.

One commentator says the battle is between Mr Berisha as an old-fashioned populist and Mr Rama as a post-modern one. Mr Berisha points to the communist roots of the Socialist Party. Mr Rama says that, though his opponent won election in 2005 on a clean-hands ticket, he has become the "incarnation of corruption". But Mr Berisha and his supporters brush off such accusations. They say the mayor is protected by media friends. The opposition retorts that the Albanian press has linked members of Mr Berisha's family with almost every recent scandal. A former defence minister has just been charged with abuse of power; the foreign minister has been charged with corruption. Sometimes you cannot see a division between public and private offices, says Albert Rakipi, of the Albanian Institute for International Studies.

Genc Pollo, the deputy prime minister, defends his government's record. He says that Albania is not the same country as before: last year GDP growth was 6% and even this year it may be 4%. Schools and roads are better. Yet the financial crisis is hitting textiles and mines, as well as remittances from the diaspora. Nervous Albanians are withdrawing savings from banks. Opinion polls are unreliable and often contradictory. What is certain is that this will be a dirty and exhausting campaign.

Charlemagne

Europe's family squabbles

Feb 26th 2009
From The Economist print edition

The sharp divisions that exist within the European Union family

Illustration by Peter Schrank



EVERY unhappy family is, as Tolstoy said, unhappy in its own way. The same goes for rows within the European Union. And, as with any extended family, you need to know your history to understand why minor rows turn into nasty fights. Behind each stand-off lies years of accrued grudges and slights.

Right now the air is filled with talk of divisions between long-standing EU members and more recent arrivals from the ex-communist block. There is both less and more to this fighting rhetoric than at first appears. As the economic crisis deepens, the European ship is "rocking", and "they're going to start throwing the weaker passengers overboard," Poland's prime minister, Donald Tusk, thundered recently. Mr Tusk is so concerned about solidarity that he has invited eight other ex-communist countries to a pre-summit meeting on March 1st, hours before all 27 EU heads of government assemble in Brussels.

Certainly, east-west divisions yawn wide right now. Ask east European ministers what the summit on March 1st is for, and they talk of the need to defend single-market rules, open labour markets and competition. Many still seethe over suggestions by Nicolas Sarkozy, France's president, that state aid for French carmakers should depend on a pledge to keep jobs in France.

This week Mr Sarkozy was in Rome with the Italian prime minister, Silvio Berlusconi. Italy and France would present a common vision at the March 1st summit, Mr Sarkozy vowed. Both believe that competition rules should support the creation of European industrial champions, and not the wholesale offshoring of jobs. America was "rightly" defending its industry. Perhaps Europe should do the same, said the French president.

In similar vein, Germany's employment minister, Olaf Scholz, assured the newspaper *Bild* that "now is not the time" for Germany to scrap its legal restrictions on workers moving freely in from countries that joined the EU in 2004 and 2007. "Jobs are under threat," said Mr Scholz, without explaining how making life harder for migrant Poles would offset plunging industrial output. On February 23rd EU foreign ministers failed to agree upon a European Commission plan to spend €5 billion ($6.4 billion) on infrastructure, notably connections for European energy grids. Southern countries such as Spain, Portugal and Greece objected that the list was skewed towards projects in the east. And Robert Zoellick, the World Bank boss, has fretted publicly that 20-year-old divisions within Europe could reopen unless west European governments back international plans to recapitalise eastern Europe's banks, and stop encouraging their

banks to pull money back from struggling branches and subsidiaries.

As with many family disputes, not every threat is equally serious. Mr Zoellick is right to worry about wobbly banks and the need for western Europe to recapitalise them. But Mr Sarkozy is isolated in his Gallic enthusiasm for a European industrial policy. France is not about to ban domestic firms from making cars in eastern Europe. Consumers are turning to the smallest, most economical Peugeots and Renaults, and those models are profitable only when made in eastern factories. Germany admits large numbers of eastern workers under quota schemes. On energy, older EU members point out that they have spent years diversifying away from Russian gas, eg, by building terminals to receive liquefied natural gas, while most ex-communist newcomers have done nothing, despite much nagging. But the big row over the commission’s energy-infrastructure scheme is actually about finance: big net contributors like Germany, Britain and the Netherlands object to a wheeze to divert money unspent in 2008.

Yet some other grudges are even deeper than they appear. The newcomers are more liberal economically than the pre-enlargement EU, on average, and more Atlanticist. Across the region, painfully young ministers, many new graduates from American universities, spent the 1990s slashing corporate-tax rates, promoting flat taxes and deregulation. In parts of western Europe that has brought charges of “fiscal and social dumping”. Less admirably, some newcomers have not cleaned up corrupt administrations and justice systems.

The ties that bind

In a family, ties of interdependence can trump even wide differences. That may yet prove true in the EU. The headlines are about western Europe’s exposure to tottering banks in the east: banks from Austria, Sweden, Italy and Greece have invested hefty sums from the Baltic to the Balkans. A prompt bail-out could solve this problem. But it will not cure opposition to enlargement. Austrian voters are among the most hostile, thanks to what one Austrian diplomat admits has been “disastrous” communication of enlargement’s benefits. Yet if Austrian banks were not on the hook for hundreds of billions of euros, public opinion might be happy to see eastern neighbours simply go bust. As it is, the Austrian government is pressing for rescue plans to extend even beyond countries in the euro. Similar calls can be heard from Sweden and Finland, which have invested heavily in the Baltics.

The most serious division now may be between countries inside the EU and countries outside. Ukraine and Russia face a grim 2009, economically. Yet both seem headed for a fresh row over gas, possibly this spring, says Vaclav Bartuska, a Czech ambassador who acted as an EU negotiator with the Russians and Ukrainians in January. Both countries believe they had a “good crisis”, scoring points off each other. They fail to see how disastrous their timing was, since one or both may yet need international help. “If Russia and Ukraine fell off the end of the Earth, many in western Europe would cheer,” says Mr Bartuska.

Europe can expect much unhappiness this year. Interdependence will cause some, as economies pull each other down. But the same ties may persuade Europeans to avert a graver peril: the notion that they can safely refuse to help one another out.

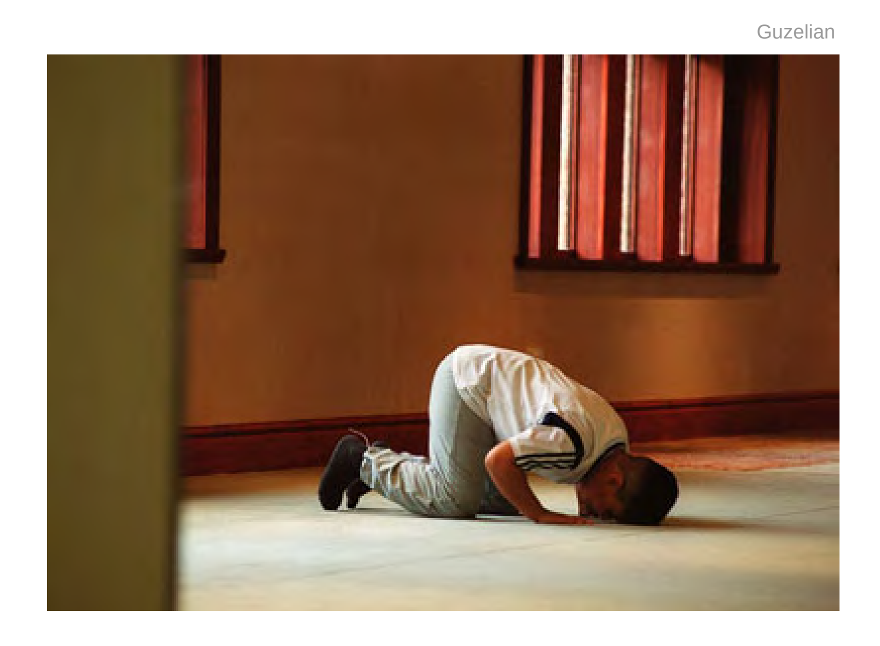
Britain and its Muslims

How the government lost the plot

Feb 26th 2009
From The Economist print edition

A desperate search for a new policy towards Islam has yet to produce results

Guzelian



A WAR, a riot, a terrorist attack or a row over blasphemy: not long ago, Britain's government knew exactly what to do when a crisis loomed in relations with the country's Muslims. As recently as July 2005, after bombs in London killed 56 people, Tony Blair was confident that he could avoid a total breakdown of trust between Muslim Britons and their compatriots.

Using an old formula, the prime minister called in some Islamic worthies and suggested they form a task force on extremism. Then, hours before the worthies were due to reconvene and mull their response, Mr Blair breezily announced that a task-force of top Muslims had just been created. They moaned, but dutifully went to work.

That system of trade-offs, the equivalent of the "beer and sandwiches" once used to woo trade unionists, had some big drawbacks. It gave hardline Muslims—generally male, old and new to Britain—disproportionate sway. It also led to some dubious bargains; for example, Muslim resentment of British foreign policy was parried by, in part, huge generosity towards the cultural demands of some Muslims—such as the right to establish schools where the curriculum bears scant relation to the lessons other young Britons get.

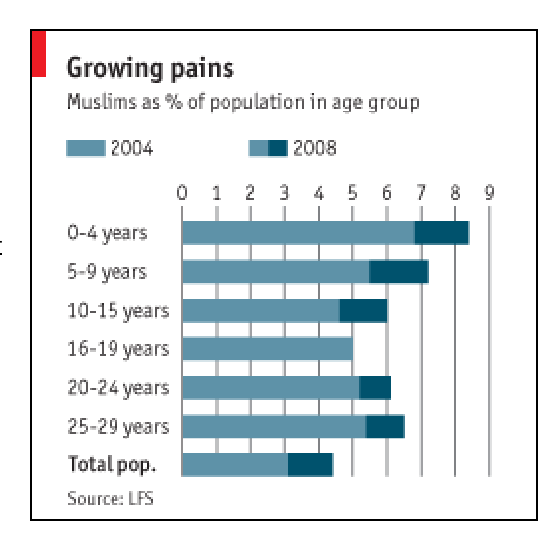
But in its own odd terms, the old system "worked". Messages could be relayed between the corridors of power and the angriest and poorest parts of the Muslim street; and Muslim leaders could be induced to expend personal and political capital urging their flock to co-operate with the police and provide useful information.

Now that system, and its unspoken compromises, lies in ruins. It was jettisoned in the autumn of 2006, when the government downgraded existing ties with the Muslim Council of Britain (in which movements close to the Muslim Brotherhood and the Islamists of Pakistan were strongly represented) and tried to find different interlocutors.

But attempts to define a new policy towards Islam in Britain have been floundering since then. The Muslim population is in many ways diverging still more from the mainstream. With its large, young families, it is also growing much faster (see chart): there are 2.4m Muslims today, according to the Labour Force Survey; the census of 2001, a rather different measure, put it at 1.6m. The government is under fire from

the political centre-right for being too soft on radical or reactionary Muslim groups who stop just short of endorsing violence. It is also attacked from the left (Muslim or otherwise) for using the fight against terrorism as an excuse for a general assault on Muslims and their cultural rights.

Hazel Blears, the communities secretary, sought to clarify official thinking in a speech on February 25th, after a stream of reports that the government was about to launch an ideological war against illiberal or extremist ways of thinking, even if they were not directly associated with violence. The government, she said, would reserve the right to deal with people whose ideas were unpleasant through a "spectrum of engagement, carefully calibrated to deal with individual circumstances". With groups that have "an equivocal attitude to core values such as democracy, freedom of speech or respect towards women" there might be "some scope for limited engagement", the minister carefully added. But on certain forms of "absolutely unacceptable behaviour"—such as homophobia, forced marriage or female genital mutilation—the government would firmly enforce the law with no regard for a cultural "oversensitivity" that had gone too far.



Her speech suggests that a debate within the cabinet on which war to prioritise—the one over ideas and values or the one against terrorism—is unresolved. The government wants to keep its options open.

But the failure of current policies aimed at fostering moderate Islam can hardly be overstated. After spending lavishly on a strategy called Prevent that was supposed to empower moderates—at least £80m ($116m) will have been dished out on such efforts by 2011—the very word "prevent" has become discredited in the strongholds of British Islam, which include east London, Birmingham and a string of northern industrial towns. At the Muslim grass roots, there is a sense that any group or person who enjoys official favour is a stooge.

Many in the government, meanwhile, think their partners are not delivering value for money. The whole relationship has deteriorated since August 2006. After a foiled plot to blow up transatlantic flights, and amid huge ire over the war in Lebanon, a group of prominent Muslims, including two now in government, signed an open letter arguing that British foreign policy in general, and its softness towards Israel in particular, was an important factor behind a surge in extremist sentiment.

Tripping up

Nearly three years on, the government's biggest problem is that it is struggling with two big questions at once. One is the set of problems described under the catch-all term of "cohesion"—narrowing the social, economic and cultural gap between Muslims (especially in some poor urban areas of northern Britain) and the rest of society. The second is countering the threat from groups preparing to commit violence in Britain or elsewhere in the name of Islam.

The government says the two problems are related: poor, frustrated and mainly self-segregated groups are more likely to produce terrorists. Muslims as a group lag behind other Britons in qualifications, employment, housing and income (see chart). But in fact the overlap between exclusion and extremism is messy. And attempts to fight terrorism through tougher policing, which can alienate whole communities, make boosting cohesion harder.

Among those who claim to speak for disadvantaged Muslims and articulate their grievances, there has been an outpouring of indignation over the government's stated aim of "preventing violent extremism" by making Muslim communities more "resilient" and better at dealing with hotheads. The idea seems to stigmatise all Muslims, many complain, while the violent extremism of, for example, the white far right is ignored.

Another gripe is that the Prevent programme has poisoned relations between central government and the city councils

through which the money is channelled. Some say councils are being strong-armed into carrying out “community” programmes that are really thinly disguised police and intelligence work.



In Birmingham the council’s loudest activist, Salma Yaqoob, complains that Prevent money goes only to those who avoid suggesting that British foreign policy helps to foment extremism, even though the link obviously exists. (Indeed, a government security minister, Lord West, admitted in January that to deny it was “clearly bollocks”.) Resentment of the gag was exacerbated by the recent Israeli assault on Gaza. Many Muslims followed it on Middle East-based media that presented an even gorier picture of Palestinian suffering than other British viewers saw.

The Gaza crisis also triggered a round of name-calling within the world of British Islam that has laid bare a rapid diminution of the middle ground on which emollient types hope to stand. Senior Muslims at the Quilliam Foundation, a “counter-terrorism think-tank” which has received nearly £1m in funding from the home and foreign offices, issued in January a denunciation of Israeli actions that was mocked as faint-hearted by more radical Muslims, while voices on the political right questioned whether the government’s “investment” in this body was paying off.

Torn between remaking the Muslim community—a task that turns out to be much harder than the designers of the Prevent strategy ever imagined—and simply fighting terrorism, the government, understandably, feels it can hardly be expected to abandon the latter. Probing and pre-empting attacks by Muslim extremists is now understood to occupy about 75% of the energy of the British security services, who claim to have had some success in reducing the number of terrorist plots that are stopped only at the last minute. Another less obvious factor in British thinking is strong American concern over the risk that a British-born Muslim could enter the United States and commit a terrorist spectacular there. A healthy slug of America’s anti-terrorism spending goes to forestall just such a possibility.

Meanwhile a string of high-profile court cases involving terrorist conspiracies has served to increase the emotional chasm between Muslim Britons and their compatriots. As an example of two worlds diverging, take reactions to the plight of Binyam Mohamed, an Ethiopian who sought asylum in Britain and was later incarcerated in Guantánamo Bay. He says he was tortured by his American captors, with help from the British secret services.

Mr Mohamed returned to Britain on February 23rd, to mixed reviews. For Muslims (and human-rights campaigners on the secular left) his saga is a tale of American brutality and British collusion. In the rambunctious popular press, however, he is portrayed as a nuisance whose presence in Britain will burden the taxpayer and waste the security services’ valuable time in surveillance.

A way forward

For all the problems besetting British Islam, however, there are plenty of individuals who exemplify at least part of the solution. Among them—at least until the recession makes it harder for strivers to climb out of poverty—are successful young professionals and entrepreneurs, often women, who have managed to fly high in business, medicine, accountancy or the media. “We have prevailed in a two-fronted struggle” against social conservatism and discrimination, says Saeeda Ahmed, the founder of a social-affairs consultancy in the north (to hear an interview with Miss Ahmed, see article).

But successful British Muslims as well as poor ones resent the fact that the rest of society often sees them mainly as potential extremists. Sarah Joseph, a convert to Islam who edits the glossy monthly *Emel*, says Muslims are fed up with being asked if they are against violence; they want people to know what they are for, such as social justice. The sad fact, in a country that has come to live in fear of terrorism, is that many Britons are indeed more interested in assessing Muslims’ potential for violence than in anything else about them.



Freedom of information

For their eyes only

Feb 26th 2009
From The Economist print edition

No, you can't know why the cabinet decided to invade Iraq

Bloomberg

EVER since Britain joined the American-led invasion of Iraq in 2003, those opposed to the war have explored all avenues to discover just how the decision to do so was reached. One of those avenues has now been blocked. On February 24th the government vetoed rulings by official freedom-of-information watchdogs that it should release the minutes of two cabinet meetings just before the invasion.

It is the first time since the Freedom of Information Act came into force in 2005 that the government has invoked a clause allowing it to refuse to comply with a ruling of the Information Tribunal. Even Labour MPs had slunk from the House of Commons by the time the decision was announced. No appeal against the veto is possible, although there is a slim chance that a judicial review may be sought.

Campaigners had hoped to learn more about cabinet deliberations on the lawfulness of invading Iraq without UN authorisation. At around the time of the two crucial meetings, the attorney-general provided two separate legal opinions, ten days apart. The first expressed reservations; the second was more gung-ho. How much did ministers know about Lord Goldsmith's initial caveats? How free were they to question the basis for his opinions?

The controversial case began in 2007, when a member of the public, turned down by the Cabinet Office when he asked for minutes of the meetings, applied to the information commissioner to require their release. The commissioner, Richard Thomas, agreed that the public interest in knowing what legal advice had been placed before cabinet outweighed the government's concerns about undermining the confidentiality of cabinet deliberations. The government appealed to the Information Tribunal, and lost. Short of complying, that left ministers with two options: appealing to the High Court to overturn the tribunal's ruling, or vetoing it. They chose the more certain one.

The cabinet, said the justice secretary, Jack Straw, had also based its decision on a calculation of the public interest. Although the minutes of cabinet meetings do not identify individuals, they are by convention kept private for fear that ministers might otherwise censor themselves, or that minuted decision-making might give way to informal discussions elsewhere. Publishing records of cabinet proceedings risked damaging British democracy itself, he said, and that risk was more serious than any posed by non-disclosure. As it happens, Mr Straw was foreign secretary at the time of the Iraq invasion.

It is unlikely in any event that the minutes would reveal much that is not already in the public domain. Since 2003 no fewer than four of the ministers who sat in cabinet then have spoken or written of the meetings. This, said the tribunal, was evidence of a dwindling respect for the doctrine of collective cabinet responsibility, to which confidentiality is said by the government to be so crucial. It also suggests that, in refusing to publish the minutes, a more serious concern for the government than the possible inhibition of free and frank debate in cabinet was the probable confirmation that on this occasion, at any rate, there wasn't any.

Bank rescues

When will we see your like again?

Feb 26th 2009
From The Economist print edition

Dismantling Royal Bank of Scotland

AT ITS obligatory roasting by the Treasury Select Committee this week, Britain's financial regulator was accused of "being responsible for supervising ten big banks and allowing five to collapse". In response, the boss of the Financial Services Authority, Lord Turner, promised a "revolution" at his organisation.

That is not far off what is taking place north of the border, at Royal Bank of Scotland (RBS), the most spectacular of those failures. Two bail-outs have left RBS majority state-owned. On Thursday, amid furore over his discredited predecessor's lavish and now taxpayer-funded pension, its new boss, Stephen Hester, provided details on plans to break up the group. He also described RBS's probable use of the government's asset-guarantee scheme, which will soon be rolled out to other banks as well. For good measure Mr Hester also announced the largest loss in British corporate history.

There is a lot to break up: acquisitive RBS was the world's largest bank by assets in 2008. Its purchase of bits of ABN AMRO, a Dutch bank, in 2007 brought the kind of geographic spread (try 20 branches in Indonesia) that looks sage at the pinnacle of a bull market and more like imperial overstretch at any other time. Mr Hester plans to split the bank into two parts: the good and the mediocre.

Into the good pot will go about three-quarters of the bank's existing activities, consisting mainly of its British and American banking operations, its insurance division and the less-dangerous bits of its investment bank, which is to be halved in size. Some tasty overseas businesses, for example in India, will be retained. The mediocre pot will contain the other foreign retail assets, which RBS will attempt to auction. But it will consist overwhelmingly of the dodgy bits of the investment bank (such as its leveraged-loan and property activities), which will probably be wound up over several years.

To bolster capital and prod the bank into lending more, the government will guarantee assets on RBS's books with a value of £302 billion ($430 billion)—equivalent to about a quarter of its total risk-weighted balance-sheet. RBS will be responsible for the first £19.5 billion of any losses, and the state for most of the rest. By limiting its risk (for a fee of £6.5 billion to the Treasury), RBS will boost its core capital ratio from 7% to 9%. It also promises to lend £50 billion more in the next two years, expanding its domestic loan book by a fifth.

That punchy rate of growth helps explain the biggest surprise. The Treasury is investing a further £13 billion which, like the guarantee fee, will take the form of a new kind of preference stock that can be converted to ordinary shares. This stock will bolster capital more securely than the suspect hybrid stuff that American regulators are keen to inject into banks (see article), since its dividends can be cancelled. The result will be that RBS's core capital ratio hits a whopping 12.4%, about double the level at JPMorgan Chase, America's soundest big bank.

All of which may seem overgenerous, particularly since the state's voting rights will be capped at 75% of the total—less than its likely financial stake in the business. But the advantages to taxpayers of having a bank that is well-capitalised enough to lend, but also well-run enough to be sold back to private investors one day, should not be underestimated.

Royal Mail

Blame the messenger

Feb 26th 2009
From The Economist print edition

Part-privatisation of an ailing business will test an ailing government's strength

WHERE Margaret Thatcher feared to tread, Peter Mandelson is rushing in headlong. The Tory prime minister, so keen to sell off nationalised industries, drew the line at Royal Mail, reputedly because its stamps bore the queen's head. Labour's business secretary does not share that quixotic attachment to a wholly publicly owned postal service, not least because it is now in such bad shape.

In a bill published on February 26th, Lord Mandelson set out proposals to sell a minority stake in Royal Mail to a private operator. The argument for the plan is straightforward. The business is facing increased competition even as the postal market buckles because of e-mail and text messaging. Adam Crozier, the chief executive of Royal Mail, told a committee of MPs on February 24th that mail volumes would shrink by 8% in the year starting this April, pushing down revenue by £560m.

Lord Mandelson believes that a private partner will inject not just extra resources but also the know-how needed to turn the business round. The scope for improvement is clear. Nigel Stapleton, the chairman of Postcomm, which regulates the business (a role that will pass to Ofcom), said this week that Royal Mail was about 40% less efficient than the best operators.

One European company that has already expressed its interest in entering into a "strategic partnership" with Royal Mail is TNT. The Dutch postal firm is, like Royal Mail, responsible for providing a universal service at home. But unlike its British counterpart it has long been run as a private rather than a public company, and it has extensive international as well as domestic operations.

One hurdle to any deal would be Royal Mail's pension scheme, which is awash in red ink. The deficit in the plan, estimated at close to £6 billion a year ago, is now expected to reach between £8 billion and £9 billion this March. No private operator will venture near that crippling liability, which the government will have to shoulder.

But the bigger obstacle will be political. Postal workers have already staged a protest in Westminster, and trade unions are up in arms. More potent still, over 130 Labour MPs have declared their opposition. If they match intent with deed, this would be easily the biggest rebellion Gordon Brown has faced since becoming prime minister in 2007, approaching the 139 Labour MPs who voted against Tony Blair over the Iraq war in 2003.

Anything involving privatisation or promoting market forces in public services has tended to be particularly fissile with backbenchers, points out Philip Cowley of Nottingham University, a chronicler of Labour revolts. Backbenchers are especially vexed that, at a time when the government has nationalised banks, it wants partially to privatise Royal Mail.

For Lord Mandelson, that may well be the point. He is anxious that the party he helped to reform along with Mr Blair and Mr Brown does not return to its old Labourite roots. His plan for Royal Mail faithfully follows the New Labour formula, in which the public realm works with, rather than against, the private sector.

Even so the government's resolve may falter. True, it could still get its way thanks to support from the Conservatives, who have already made it clear that they will back the bill. But that would present to the electorate a sorry spectacle of an end-of-term government in hock to the opposition. Despite the merits of Lord Mandelson's plan for Royal Mail, messy compromises with Labour rebels look inevitable if it is to get anywhere.



Needle disposal

Yes to heroin, insulin no

Feb 26th 2009
From The Economist print edition

Britain is a pioneer in needle exchange—but only for lawbreakers

IN MOST drugs league-tables, Britain fares poorly. More cocaine disappears up British nostrils than any others in Europe and cannabis is likewise more popular. But amid the gloom there is a success story. Britain's 200,000 or so injecting drug abusers are relatively unlikely to pick up an illness from their habit, thanks to the free needle-exchange services that have existed since the 1980s. These allow them to collect clean needles and ditch their old ones with no questions asked. That is one reason why fewer than 2% of injecting addicts in Britain are HIV-positive. (In Spain, by contrast, which came round to the idea of exchanges much later, more than 20% have the illness.) On February 25th the National Institute for Health and Clinical Excellence (NICE), an official advisory panel, recommended that such services be made more widely available.

Oddly, one group of drug-dependants has a tougher time getting and disposing of their needles: diabetics. The 250,000 Britons who have type-one diabetes, and about a third of the 2.3m with type-two diabetes, shoot up with insulin several times a day. Among them they get through almost 900m needles a year. But whereas illicit drug users can pick up needles and sharps bins freely over the counter in many pharmacies (and in a choice of colours, to prevent accidental sharing), diabetics need a doctor's prescription (for which, at least, there is no charge).

If that seems mildly unjust, it gets more so when diabetics try to dispose of their needles. "I'm terribly sorry. Unless you've used them for illegal drugs, we're not allowed to take them," says one London pharmacist. Under a needle-exchange initiative she is paid by the local health authority to get rid of needles handed in by illicit drug users, but not by diabetics and other patients. Health bosses have even told her off for accepting needles from non-junkies—and it is clear when she does, because addicts are given black boxes but diabetics yellow ones. "Maybe we could take them out and swap them round," she offers. "Or you could just pretend to be an addict," suggests a pharmacist in a different borough.

Some health authorities give pharmacists sufficient funding to take needles from all comers. Others say that doctors should accept them, as it is they who prescribe the treatment. But many surgeries refuse to take the needles, even when the health authority is willing to pick up the tab. One doctor frets that patients might leave needles on the pavement outside her surgery if they found it shut after hours. Others say they haven't the space to store all the boxes. Many GPs believe that it is the job of pharmacists—and vice versa.

Ultimate legal responsibility lies with local councils, which are obliged to offer a home-collection service on request. But they are entitled to charge: £28.09 is quoted by one London borough for the collection of five one-litre boxes. Given that prescriptions of needles are free, it is odd that their safe disposal is not, points out Diabetes UK, a charity. It reports a "postcode lottery", where the ease of disposal varies widely by locality.

NICE has never provided guidelines on needle disposal for licit drug users. If it did, it might find cost-savings to recommend: making disposal easier is probably cheaper than clearing up needles that are illegally dumped, and letting people use their local pharmacy might cut down on expensive home collections. Until then, how many illicit needle-exchange clients are diabetics in disguise?

Depression architecture

Uplift from downturn

Feb 26th 2009 | MANCHESTER
From The Economist print edition

The last severe recession left a lasting legacy. Will this one?

IMAGES of the Great Depression in Britain are dominated by grim pictures of rivers of cloth-capped unemployed men and, iconically in the north of England, newsreels of the march of the workless from Jarrow to London. Yet the more durable legacy of the 1930s encompasses some of the most stunning examples of British public architecture, as well as the advent of high-street shopping as a leisure activity.

Newcastle's arching Tyne Bridge, Liverpool's modernist Philharmonic Hall and the classical rotunda of Manchester's central library, which held 300 readers in what was then the country's biggest reading room outside the British Library in London, were all products of the civic and, in some cases, philanthropic determination of local leaders. They wanted not only to provide work but also to transform their cities in the process.

Charlie Wildman, a historian at Manchester University, says the hardships of the times spurred an outburst of creativity. Liverpool, for example, is home to some of Britain's best Art Deco design, in the Queensway tunnel under the Mersey, the Royal Court theatre and the city's first airport terminal. The new style's clean lines, a reaction against Victorian ostentation that gave post-war austerity a distinct aesthetic, were enthusiastically adopted by department-store chains such as Marks and Spencer and John Lewis. (The Depression was also responsible for the latter's current corporate structure: John Spedan Lewis was appalled at the "perversion of capitalism" that increased the disparity between his family's wealth and the surrounding poverty, and turned his business into a profit-sharing co-operative.)

This was, too, the era of suburban expansion. City grandees such as Lord Simon of Wythenshawe, heirs to Victorian philanthropic ideals, bought large tracts of land for municipal housing. Manchester's city council gratefully accepted Lord Simon's gift of land and, after battles with the authorities of neighbouring Cheshire, built the model garden suburb of Wythenshawe. By 1939 it had 40,000 residents in 8,145 houses (though more recent inhabitants find plenty to criticise). Liverpool, for its part, shifted 140,000 people into 33,355 suburban homes during the interwar years.

The suburbanites took to city-centre shopping in a big way because the improvers' investment in tramways made it cheap and easy for them to travel into town. There, the impressive interiors of the new emporia, an approach brought to Britain in 1909 by the Chicago retailer Gordon Selfridge, and their external grandeur helped to convert the Saturday shop from a dreary task into something far more enjoyable.

So may Britons hope to have their cities dramatically improved this time around by official attempts to breathe life into a moribund economy? Gordon Brown undoubtedly has economic rescue in mind, but somehow widening the M25 and cutting the VAT rate seem unlikely to leave quite the same aesthetically pleasing mark on the landscape.

Bagehot

The price of freedom

Feb 26th 2009
From The Economist print edition

Are civil liberties affordable during a recession?

Illustration by Steve O'Brien



A MOB of Britain's finest eccentrics will gather in central London on February 28th. Their ranks will include outspoken novelists, radical lawyers and fed-up judges. David Davis, an unusual MP who left the shadow cabinet to wage guerrilla war from the backbenches, will be there; so will Shami Chakrabarti, the relentless head of Liberty, a pressure group. Several of those attending can sometimes seem pious; but in a stubborn, deeply English way, many are rather magnificent. The occasion is the "convention on modern liberty", an event designed to rally opposition to the ongoing erosion of rights and freedoms in Britain (there will be similar meetings in other cities).

It might not seem the best moment for the ragtag gang to make its stand. The hour of the leviathan is nigh: the financial crisis has given the state permission to meddle in places that would once have seemed indecent. Economic "fairness" has eclipsed most talk of the judicial kind. Even in the fat times, often it was only the eccentrics who seemed to care about *habeas corpus*, due process or the use of anti-terrorist laws to quell hecklers at the Labour Party conference. Surely the slump is not the time to reclaim liberties that were casually cancelled during the boom?

Precedents in Britain and elsewhere do indeed suggest that freedom often contracts in line with GDP. People get angry. They misbehave: crime may rise, as a leaked Home Office memo predicted last year. They march, demonstrate and occasionally riot: newspapers this week reported lurid police warnings about a forthcoming "summer of rage". They become more susceptible to extreme, xenophobic voices: there is widespread anxiety in British politics about a breakthrough by the loathsome British National Party at the European elections in June. Capturing a Euro-seat would represent a triumph for the far right greater than any achieved by Oswald Mosley and his blackshirts in the 1930s.

The big risk to civil rights could come in the way the government responds: in the methods it uses to contain the wrath, to cater to it and to distract the wrathful. It would, sadly, be unsurprising if ministers were to echo far-right rhetoric about immigrants instead of wholeheartedly repudiating it; they might tout even more inhumane policies towards asylum-seekers and terrorist suspects. Demos may be met with harsh counter-measures (Liberty was formed to protest against police treatment of the "hunger marchers" who came to London during the Depression).

Any such crackdowns will have to be orchestrated on a tight budget. But that might make them harsher: a home secretary who can't afford to recruit police officers might instead give the ones she does have yet more intrusive powers. As Mr Davis satirically puts it, "if you can't stop violent crime, at least make

bloodcurdling noises about what you'll do to the few violent criminals you do manage to catch."

Eternal vigilance

That is the gloomy prognosis for civil liberties in the lean years. Yet there is a rosier one. To begin with, even if penury encourages ministers to take shortcuts, a lack of cash for security projects will help. The technology of unfreedom is costly: number-plate recognition systems, identity cards and the government's assorted, panopticonic databases of DNA and other information are hugely expensive (always much more so than is at first estimated). They will be a much harder political sell when spending in other areas is being cut. Faith in such databases has anyway been undermined by civil servants' unfortunate habit of leaving discs and computers on trains, by the pool, etc.

That incompetence has contributed to a general loss of confidence in government. The campaigners' hope is that, as public disenchantment sharpens, it will take in a scepticism about over-mighty criminal-justice policy as well as about economic oversight. And the downturn, some say, may make liberty seem more precious rather than less. Two foreign holidays a year and the odd flat-screen television, the argument runs, may once have represented ample freedom for many. Britons may care more about, say, the abuse of surveillance powers by local councils when their bank accounts give them less freedom to shop and travel.

The hope, in other words, is that voters will prove able to think about more than one issue at a time. Conversely, the government may be too embroiled in the economic mess to waste time in Parliament and use up the ebbing goodwill of Labour MPs on illiberal measures. The abandonment, last autumn, of its bid to ram through an extension of pre-charge detention for terrorists could be a case in point. Gordon Brown himself has had a somewhat anguished relationship with such initiatives, seeking to justify them intellectually even as he exploits them politically. The recession offers ample cover for him to ditch some (ID cards, for example) without losing face.

As for the Tories, they are recent and wavering converts to the eccentrics' cause. Chris Grayling, the new shadow home secretary, has made manly noises about wanting "fewer rights, more wrongs". Other leading Tories are privately more authoritarian than their party's officially liberal line. But they have made some commitments—to scrap ID cards, for example—that will be difficult to disavow, if and when they take office. The Liberal Democrats, who have assorted ideas for unwinding Labour's nastier inroads on liberty, should help to keep them honest.

The credit crunch has shaken the kaleidoscope of British politics. Banks have been nationalised; ridiculed leaders have been lionised, then ridiculed again. It will doubtless have further unpredictable side effects—including, maybe, a creeping victory for the eccentrics. Perhaps rights and liberty will remain a marginal concern, which few in a pinched Britain have the time or inclination to worry about; yet it may be the price of restricting freedom that proves too high for politicians. Liberty could turn out to be one of the few things that prosper in the slump.





Proliferation

United in defiance

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From The Economist print edition

The proliferation chain that links North Korea and Iran

AP



THE final frontier is being assaulted by a couple of troubling pioneers. North Korean officials are boasting that they will soon launch a rocket that will lift a communications satellite into space. With this defiant spectacular, they seem to be cocking a snook at America, South Korea, Japan, China and Russia, who have been trying through six-party talks to curb North Korea's equally vaunted nuclear-weapons efforts. Meanwhile, earlier in February, Iran—suspected of harbouring similar nuclear ambitions to North Korea's, though it denies this—lifted its own small, supposedly home-made satellite into orbit too.

Both regimes trumpet their space prowess, and indeed such technological feats are not easy to achieve. But how do these "civilian" space efforts complement their terrestrial nuclear work? That is the question that deeply worries outsiders.

India showed the way: its supposedly civilian space programme sometimes won generous outside assistance, even as nuclear help was denied for fear of advancing its suspected weapons-building. As a result of the parallel effort, India now has missiles capable of delivering nuclear warheads on targets not just throughout Pakistan, but deep inside China too. Quite simply, the technology needed to lift a satellite off the launch pad and shield it from damage on its way into space is indistinguishable from that needed to launch a far-flying nuclear-tipped ballistic missile.

North Korea and Iran appear to be following suit. Kim Jong Il's regime claims to have first embarked on its space adventures in 1998, when it launched a Taepodong-1 rocket over an alarmed Japan, across the Pacific towards a startled America. Mr Kim even issued a stamp to celebrate what was said to have been the successful launch of a satellite that had since been warbling patriotic tunes back from space. Oddly, no one else ever picked up its signal. A failed missile test, concluded America, after watching the rocket plop down in the Pacific.

Whether the satellite was a figment of Mr Kim's imagination hardly matters. The latest promised test-launch will violate resolution 1718, which bans North Korea from all such activity. This was passed by the United Nations Security Council in 2006, unusually with China's backing, after North Korea first tried (but failed) to launch a still more capable missile and then conducted what is thought to have been its first nuclear test. Its determination now to carry on launching regardless has led to speculation in some

quarters that the missile, assuming it launches successfully, could even be shot down by the new ballistic-missile defences that Japan and America have been frantically cobbling together to protect Japan from North Korea's missile threats.

Mr Kim seems to be using his missile preparations to grab the attention of the new Obama administration in America, and to raise the ante in the six-party nuclear talks. These have been stalled for months because of North Korea's refusal to accept proper verification of its nuclear programmes; that will remain the case—or so the other five parties suspect—until the regime in Pyongyang squeezes extra goodies out of the Americans.

The test, if it goes ahead, will also roughly coincide with an annual joint military exercise between America and South Korea, at a time when relations between South and North have deteriorated badly. The North Korean media claim, not for the first time, that the two Koreas are at "the brink of war", and that America is preparing a pre-emptive strike against the North.

Certainly Mr Kim is determined to look as threatening as possible. Writing in the *Washington Post* on February 19th, Selig Harrison, who is a frequent visitor to North Korea, said that the foreign-ministry and defence officials he talked to recently had left him with the impression that North Korea's stash of plutonium (which is exhibit-A in the six-party talks, though there are lingering concerns that Mr Kim has also dabbled in enriched uranium, another possible bomb ingredient) had already been "weaponised"—that is, converted into missile warheads.

If that is the case, then North Korea's "satellite" test will be doubly alarming. Although the 2006 nuclear test was thought to have fizzled, it may nonetheless have helped North Korea master a design for the sort of smaller warhead that a missile could carry.

But there is a further, bigger, worry even than Mr Kim's theatricals. North Korea and Iran have long been collaborating on building missiles; the two are thought to have worked together in Iran to improve on basic North Korean missile designs at times when it has been impolitic for the North to test for itself. Iran has learned a great deal from this work; recently it has been making strides in its own missile technology. No one knows whether this collaboration has included warhead or other nuclear work too (though North Korea appears to have helped Syria to build a suspected and almost completed plutonium-producing reactor, which Israel destroyed in an air raid in 2007).

Strutting its stuff

North Korea is evidently quite happy to brandish its bombs. It flounced out of the Nuclear Non-Proliferation Treaty back in 2003 after evidence emerged that it had been cheating on an earlier denuclearisation deal with America. Iran, by contrast, claims to be an NPT member in good standing. It insists that it has no use for nuclear weapons, and that all its nuclear activities, including a uranium-enrichment effort that continues to expand in defiance of UN Security Council resolutions and sanctions, are entirely peaceful in intent; the uranium, it says, is simply intended to fuel a future fleet of power stations.

Nothing if not brazen, it claims backhanded vindication in a controversial National Intelligence Estimate by America's spooks, which concluded a little over a year ago that Iran had indeed had a bomb programme, but that it had stopped in 2003 when its formerly secret uranium activities came to light. But what that report failed to explain clearly was that Iran was continuing work quite openly on the two other necessary components of a weapons programme: first, uranium enrichment (with a bit of time and redirection of piping, low-enriched uranium can easily be turned into the highly enriched sort needed for a bomb) and efforts to produce plutonium; and second, the efforts under way for the development of a missile that could carry a nuclear warhead.

AP



Bushehr: no need for Iran's enriched uranium here

Iran is the only country so far to have built a uranium-enrichment plant before having even a single working reactor that would need its uranium as fuel for the reactor core. Even a Russian-built reactor at Bushehr that is now being put through its technical paces before coming on-stream later this year will operate on Russian-supplied fuel. Nor does it have sufficient uranium ore of its own to sustain a large-scale enrichment effort. Since uranium exports to Iran are prohibited by UN sanctions, its only option eventually will be to import more of the stuff illegally, using the nuclear black market that enabled it to get secretly started in the uranium business.

Nonetheless, Iran has just passed another nuclear milestone. According to figures contained in a new report circulated to the 35-nation board of the International Atomic Energy Agency (IAEA), the UN's nuclear guardian, ahead of a meeting that opens on March 2nd, Iran has accumulated an unexpectedly large amount of low-enriched uranium—enough, says the Washington-based Institute for Science and International Security, for Iran to be confident that, should it proceed with further enrichment, it will have sufficient material for a single nuclear weapon.

What is more, the agency reported a big discrepancy (about 30%) between the amount of uranium Iran had earlier said it was producing and the amount now stockpiled. It is often hard to guess the real output of enrichment centrifuge machines, like Iran's, in their first stages of operation. However, in the view of other experts, even rough calculations based on earlier figures should have told inspectors that the Iranian estimate was far too low. The IAEA is confident that all the enriched uranium is properly safeguarded. But safeguards are something Iran disregards when it suits.

There have long been suspicions that Iran may be engaged in a parallel, possibly military, enrichment effort: in April 2006 without notice to inspectors, it removed and then put back a cylinder of the gas from which enriched uranium of either sort is spun, so that inspectors briefly lost track of the material it contained. When they were subsequently measured, the cylinder's contents were deemed to be correct within an acceptable margin of error. But that does not rule out the possibility that a small quantity of the gas, calculated to fall within that error margin, was diverted to test some hidden centrifuges.

As the IAEA's latest report makes clear, Iran is also refusing them access, as required under its safeguards obligations, to the site where it is building its own plutonium-producing reactor, one that just happens to be ideally sized for making bomb material. And it will not answer increasingly pointed questions from inspectors about studies and other information provided by several governments that appear to show weapons-related work on uranium conversion, on high explosive testing for nuclear-trigger devices and—the evidence behind the doubts about Iran's "space" programme—on development work to redesign the inner cone of a re-entry vehicle for Iran's Shahab-3 missile, so as to accommodate a nuclear warhead.

North Korea's neighbours may be prepared simply to huddle together, trusting in the best efforts of diplomacy and missile defences. But countries in the vicinity of Iran are becoming more agitated. Israel's probable new prime minister, Binyamin Netanyahu, has said a nuclear Iran poses a far graver threat than the global recession.

So Barack Obama and his new team—he has now appointed special envoys to deal with both Iran and North Korea—don't have much time to show that their promised readiness to talk directly to Iran can produce results. And unless results are forthcoming, the long-running drama over Iran's nuclear ambitions could rapidly escalate into a global crisis.


WORLD INTERNATIONAL

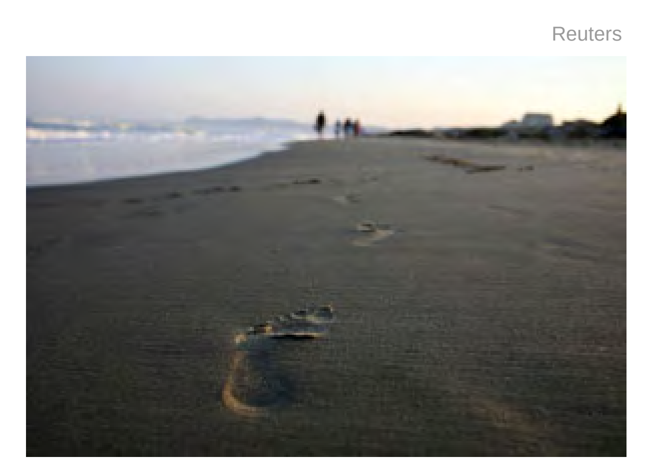
The World Bank

Guilty as charged

Feb 26th 2009
From The Economist print edition

A flawed project in Albania has highlighted some broader concerns

Reuters



A large, embarrassing footprint on Albania's sands

WHEN Robert Zoellick took over the World Bank in 2007—after months of bitter wrangling over professional favours done by its former president, Paul Wolfowitz, for his girlfriend—many people hoped that happier times lay head for the institution. So it was a shock to hear Mr Zoellick describe as "appalling" the bank's behaviour over a bungled project to develop the coast of Albania. He was responding to the findings of a bank-appointed panel which found a clear link between the wrongful demolition of 16 homes in the coastal town of Jale and the project, to which the bank had pledged $17.5m.

Mr Zoellick's frank *mea culpa* sounded impressive, and the project has been suspended. The bank management's response, in a document dated February 18th, is also contrite. And legal aid to the families affected, to help them seek compensation, has been promised.

But investigations have uncovered a sorry tale of incompetence, mismanagement, obfuscation and possibly worse. And they come barely a month after the bank was forced to issue a statement belatedly identifying three IT firms that had been debarred from bank projects—two of them, Wipro and Satyam, for providing "improper benefits" to bank staff. The imbroglio provides fresh fodder to critics of the bank who argue that it is slow, opaque in its decision-making and not sufficiently accountable to people its work affects.

In the Albanian project, this is one of the embarrassing things: an appraisal document included a crucial reference to an agreement with the government about a moratorium on the demolition of unauthorised buildings—until clear rules could be set for defining illegal activity and assisting those who were affected. In reality, no such agreement existed, something that at least some staff knew. Corrections to the document were made shortly before the project was presented to the bank's board, then amended, then inexplicably dropped. As a consequence, some staff continued to think that an agreement was in place, and to refer to it in other documents. A charitable way to describe the process would be haphazard.

According to the report by the bank's general counsel into the curious matter of the agreement that wasn't, the bank has no clear procedure to fix responsibility for the accuracy of project appraisals. The response of the management admits the need for thoroughness in preparing for board meetings. Some might call this a statement of the obvious.

The Albanian project also sheds light on some murky questions about whom the bank recruits and co-operates with when it executes projects. In this case, the bank's management told the investigation

panel at first that there was no link at all between the demolitions in Jale and the coastal-redevelopment project.

Go directly to Jale

Indeed, the demolitions were carried out by the Albanian construction police, not the bank. But the panel found that the aerial photographs which identified the targets for demolition were provided by staff in the project co-ordination unit, and that they used World Bank funds to get them taken. These photographs were then sent to the construction police, along with a letter from the project co-ordinator asking for action to be taken “as fast as possible”.

The construction police responded to the project co-ordinator’s request with alacrity, arriving in the hamlet of Jale to demolish the “illegal” houses in the early hours of the morning. This eagerness to please was probably not entirely out of respect for the World Bank: the project co-ordinator was the son-in-law of Albania’s prime minister, Sali Berisha, who has recently turned his ire on the bank.

The inspection panel notes in its report that local World Bank staff were concerned both by the co-ordinator’s political links and by his qualifications. He was appointed anyway, getting his job just a few months after his father-in-law took over as prime minister.

This is unlikely to be the only case of its kind. The appointment of influential people with their own agendas, sometimes at loggerheads with the bank’s, poses a large problem for the way its projects are administered. The bank’s response to the Albanian case includes a commitment to try to avoid appointments that involve conflicts of interest “if possible”. But the problem, some would argue, is that having such people on its projects may allow the bank to cut through red tape by virtue of their connections, a valuable “skill” in difficult political environments. And this could provide an incentive for senior managers to look the other way when well-connected people are recruited.

Old-fashioned corruption is a problem too, as is apparent from the saga of the two IT firms mentioned above. There is also a huge brouhaha about fraud in health projects in India, where investigations that ended in 2008 revealed “unacceptable indicators of fraud and corruption”, according to Mr Zoellick.

On the positive side, the bank has at least learnt to admit serious errors when they are proved to have happened. And it has wrestled seriously in recent years with the tough question of whether or not to cut off funding when corruption is suspected. Empowering its inspection panel to look into matters of corruption, which are currently not within its remit, would also be a useful step.

Talking rubbish

Feb 26th 2009
From The Economist print edition

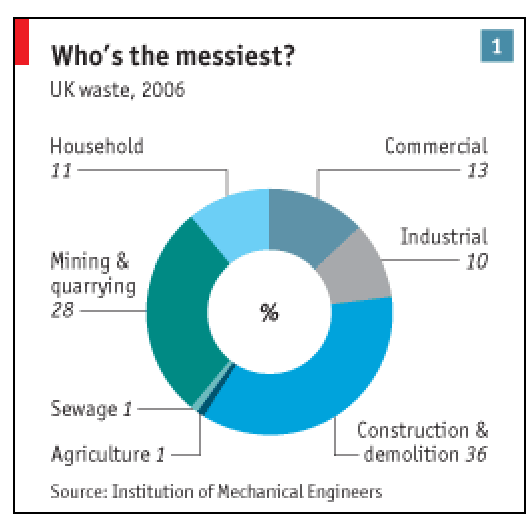
Environmental worries have transformed the waste industry, says Edward McBride (interviewed here). But governments' policies remain largely incoherent

Eyevine



THE stretch of the Pacific between Hawaii and California is virtually empty. There are no islands, no shipping lanes, no human presence for thousands of miles—just sea, sky and rubbish. The prevailing currents cause flotsam from around the world to accumulate in a vast becalmed patch of ocean. In places, there are a million pieces of plastic per square kilometre. That can mean as much as 112 times more plastic than plankton, the first link in the marine food chain. All this adds up to perhaps 100m tonnes of floating garbage, and more is arriving every day.

Wherever people have been—and some places where they have not—they have left waste behind. Litter lines the world's roads; dumps dot the landscape; slurry and sewage slosh into rivers and streams. Up above, thousands of fragments of defunct spacecraft careen through space, and occasionally more debris is produced by collisions such as the one that destroyed an American satellite in mid-February. Ken Noguchi, a Japanese mountaineer, estimates that he has collected nine tonnes of rubbish from the slopes of Mount Everest during five clean-up expeditions. There is still plenty left.



The average Westerner produces over 500kg of municipal waste a year—and that is only the most obvious portion of the rich world's discards. In Britain, for example, municipal waste from households and businesses makes up just 24% of the total (see chart 1). In addition, both developed and developing countries generate vast quantities of construction and demolition debris, industrial effluent, mine tailings, sewage residue and agricultural waste. Extracting enough gold to make a typical wedding ring, for example, can generate three tonnes of mining waste.

Out of sight, out of mind

Rubbish may be universal, but it is little studied and poorly understood. Nobody knows how much of it the world generates or what it does with it. In many rich countries, and most poor ones, only the patchiest of records are kept. That may be understandable: by definition, waste is something its owner no longer wants or takes much interest in.

Ignorance spawns scares, such as the fuss surrounding New York's infamous garbage barge, which in 1987 sailed the Atlantic for six months in search of a place to dump its load, giving many Americans the false impression that their country's landfills had run out of space. It also makes it hard to draw up sensible policies: just think of the endless debate about whether recycling is the only way to save the planet—or an expensive waste of time.

Rubbish can cause all sorts of problems. It often stinks, attracts vermin and creates eyesores. More seriously, it can release harmful chemicals into the soil and water when dumped, or into the air when burned. It is the source of almost 4% of the world's greenhouse gases, mostly in the form of methane from rotting food—and that does not include all the methane generated by animal slurry and other farm waste. And then there are some really nasty forms of industrial waste, such as spent nuclear fuel, for which no universally accepted disposal methods have thus far been developed.

Yet many also see waste as an opportunity. Getting rid of it all has become a huge global business. Rich countries spend some $120 billion a year disposing of their municipal waste alone and another $150 billion on industrial waste, according to CyclOpe, a French research institute. The amount of waste that countries produce tends to grow in tandem with their economies, and especially with the rate of urbanisation. So waste firms see a rich future in places such as China, India and Brazil, which at present spend only about $5 billion a year collecting and treating their municipal waste.

Waste also presents an opportunity in a grander sense: as a potential resource. Much of it is already burned to generate energy. Clever new technologies to turn it into fertiliser or chemicals or fuel are being developed all the time. Visionaries see a future in which things like household rubbish and pig slurry will provide the fuel for cars and homes, doing away with the need for dirty fossil fuels. Others imagine a world without waste, with rubbish being routinely recycled. As Bruce Parker, the head of the National Solid Wastes Management Association (NSWMA), an American industry group, puts it, "Why fish bodies out of the river when you can stop them jumping off the bridge?"

Until last summer such views were spreading quickly. Entrepreneurs were queuing up to scour rubbish for anything that could be recycled. There was even talk of mining old landfills to extract steel and aluminium cans. And waste that could not be recycled should at least be used to generate energy, the evangelists argued. A brave new wasteless world seemed nigh.

But since then plummeting prices for virgin paper, plastic and fuels, and hence also for the waste that substitutes for them, have put an end to such visions. Many of the recycling firms that had argued rubbish was on the way out now say that unless they are given financial help, they themselves will disappear.

Subsidies are a bad idea. Governments have a role to play in the business of waste management, but it is a regulatory and supervisory one. They should oblige people who create waste to clean up after themselves and ideally ensure that the price of any product reflects the cost of disposing of it safely. That would help to signal which items are hardest to get rid of, giving consumers an incentive to buy goods that create less waste in the first place.

That may sound simple enough, but governments seldom get the rules right. In poorer countries they often have no rules at all, or if they have them they fail to enforce them. In rich countries they are often inconsistent: too strict about some sorts of waste and worryingly lax about others. They are also prone to imposing arbitrary targets and taxes. California, for example, wants to recycle all its trash not because it necessarily makes environmental or economic sense but because the goal of "zero waste" sounds politically attractive. Britain, meanwhile, has started taxing landfills so heavily that local officials, desperate to find an alternative, are investing in all manner of unproven waste-processing technologies.

As for recycling, it is useless to urge people to salvage stuff for which there are no buyers. If firms are passing up easy opportunities to reduce greenhouse-gas emissions by re-using waste, then governments have set the price of emissions too low. They would do better to deal with that problem directly than to try to regulate away the repercussions. At the very least, governments should make sure there are markets for the materials they want collected.

This special report will argue that, by and large, waste is being better managed than it was. The industry that deals with it is becoming more efficient, the technologies are getting more effective and the pollution it causes is being controlled more tightly. In some places less waste is being created in the first place. But progress is slow because the politicians who are trying to influence what we discard and what we keep often make a mess of it.

You are what you throw away

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From The Economist print edition

The anthropology of garbage

WASTE can be a revelation. Excavations of old rubbish tips (or middens, as archaeologists call them) provide much of our knowledge of everyday life in the past. Many ancient civilisations piled up mountains of garbage. At a spot in America called Pope's Creek, on the shores of the Potomac river, oyster shells discarded by the pre-Columbian inhabitants cover an area of 30 acres (12 hectares) to an average depth of ten feet. Enormous shell middens can be found all over the world, wherever ancient migrants came across handy oyster and mussel beds.

Archaeologists have found papyruses inscribed with parts of lost plays by Sophocles and Euripides in a Greco-Roman rubbish tip in Egypt. The same site, near the ancient town of Oxyrhynchus, yielded a wealth of 2,000-year-old invoices, receipts, tax returns and other documents.

Modern waste can be equally enlightening. Dustbins generally provide a more honest account of their owners' behaviour than do the owners themselves. A research programme at the University of Arizona conducted several studies comparing the participants' own assessments of their habits with the record provided by their rubbish. It turned out that people wasted much more food than they realised, claimed to cook from scratch more often than they really did and ate more junk food and less virtuous stuff than they admitted. For example, they overestimated their consumption of liver by 200%. A survey on consumption of red meat was particularly telling. Rich households, perhaps wanting to be seen to be eating healthily, claimed to consume less of it than they did, whereas poor ones, possibly indulging in wishful thinking, claimed to eat more.

The project uncovered many other oddities of human behaviour. For example, a well-publicised shortage of a particular product actually causes people to throw more of it away, perhaps because they have bought too much of it. Similarly, a public campaign to get people to take hazardous waste to special collection points makes them put more of it in the bin. Such campaigns seem to prompt them to have a clear-out but they often do not make it to the collection point.

Don't ask, dig

Waste can be used to determine with great accuracy how many people are living in a particular place, how old they are, how much they earn and which ethnic group they come from. America's Census Bureau has toyed with the idea of using data derived from analyses of household rubbish to adjust its survey data. America's Supreme Court has also acknowledged the importance of waste, ruling that police may rummage through trash left out for collection without a warrant.

Economist.com SPECIAL REPORTS

Down in the dumps

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From The Economist print edition

Managing waste properly is expensive, which is why rich countries mostly do it better than poor ones

THERE are really only three things you can do with waste: bury it, burn it or recycle it. All of them carry environmental and financial costs, and all require careful management. At first sight burying or burning the stuff seem the simplest options, but the potentially hazardous consequences require strict controls, as this section will show. Recycling, which is a highly complicated business, will be dealt with in a later section (see article).

The very idea that waste needs to be "managed" is relatively new. Throughout much of human history waste took care of itself, and in many parts of the world it still does. In poor agricultural societies there is not much of it to begin with. Broken tools and worn clothes are repaired, food scraps are fed to livestock and so on. In such places waste is seen as having an inherent value. The reason why plastic bags blow about by the roadsides in so many poor countries, says Philippe Chalmin of the Université Paris Dauphine, is not that the local people are litterbugs but that they are frugal enough not to need a waste-collection system of any sort. Plastic bags are among the few items they cannot recycle.

Waste first became a problem in cities, where it accumulated faster than it rotted away, creating an eyesore and a health hazard. In 1552 Shakespeare's father was fined a shilling for leaving excrement in the street instead of taking it to the designated spot at the edge of town. Benjamin Franklin helped to set up America's first street-cleaning service in Philadelphia in 1757. But even in cities most items that would now be considered rubbish were collected and put to use. Human and animal droppings were gathered up and spread on fields as fertiliser. Rags were used to make paper.

Anything that had no further use was, and still is, burned or buried. To begin with, dumps were simply places where waste was left to rot with little or no treatment. At best, a layer of dirt or debris was spread over the decaying rubbish to help control smells and vermin, a technique adopted by the inhabitants of Knossos in Crete in about 3000BC.



The amount of waste a community generates tends to grow with its economy (see chart 2). Thus America produces over 700kg of municipal waste per person each year, compared with Nairobi's 220kg. The richer people get, the more paper, plastic and metals they chuck out, so the proportion of food waste goes down. Ash tends to disappear from household waste altogether as electricity and gas replace coal- and wood-fired boilers and stoves.

Buried, not gone

The increased volume of waste going to landfill causes several problems. The first one is to find enough space for it. Some countries have no trouble with that: America's existing landfills, for example, have 20 years' worth of capacity left, according to NSWMA, the industry group. The former Fresh Kills landfill in New York, at 12 square kilometres (five square miles), is the world's biggest man-made structure, dwarfing Egypt's pyramids. But in densely populated countries such as Singapore, or in mountainous places such as Japan, finding an appropriate site can be hard.

Even where plenty of land is available, locals are often hostile to landfills because of the damage they can do to human health and to the environment. Densely packed organic matter produces methane as it rots, which can catch fire or cause explosions. That is also bad for the atmosphere, because methane is a greenhouse gas 21 times more potent than carbon dioxide. The process of decay produces ammonia too, which in sufficient concentrations can poison fish and amphibians and render water undrinkable.

The changing composition of waste going to landfill also gives rise to other forms of pollution. The bacteria that break down rotting waste produce acids. In the past the high proportion of ash in household rubbish would have helped to neutralise them, but now they can be concentrated enough to dissolve poisonous heavy metals such as lead and cadmium. Water leaching through the landfill can carry such toxins into the groundwater or nearby bodies of water, and from there into drinking water and the food chain.

Western household waste is full of dangerous chemicals. There are paints and batteries containing lead; thermometers and lightbulbs containing mercury; electronic goods full of hazardous substances; pesticides from the garden; solvents for cleaning; and used motor oil from the garage, to name a few of the most common. In theory, none of these items should go into ordinary landfills. In practice, many do.

Industrial waste, medical waste and mining waste often contain toxic substances in even greater quantities and concentrations. CyclOpe estimates that the world's biggest economies produce perhaps 150m tonnes of hazardous waste a year between them, but information is alarmingly thin on the ground. Heavy metals and acids often commingle in mining waste, much as they do in ordinary landfills, and can leach into the soil and water. At the most polluted sites even the dust blown from tailings can be dangerous.

Yet the main alternative, burning waste, can be just as bad, both for people and for the planet. Smoke from incineration may carry many of the same toxic substances up the chimney and into the atmosphere. Nitrogen and sulphur in the smoke contribute to acid rain, and soot particles cause respiratory problems. In addition, burning organic waste produces chemicals called dioxins and furans, suspected carcinogens which damage the nervous and immune systems, among other ill effects, and are harmful even in minuscule quantities. After burning there is still the ash to be disposed of, usually in a landfill, again with potentially baleful consequences.

In the 1960s and 1970s a series of grisly accidents with toxic waste prompted governments in rich countries to regulate its disposal more stringently. In Japan, for example, the discharge of mercury-laden chemicals into Minamata Bay killed at least 1,000 people and made another 10,000 ill. In America a neighbourhood in Niagara Falls called Love Canal turned out to have been built on top of clay pits containing hazardous waste from a chemical factory. Following a huge rise in birth defects and miscarriages the government moved over 800 families to new homes.

Most Western governments have since imposed rules to minimise pollution from landfills and incinerators and to prevent leaks of toxic waste. Firms generally need a licence to use, transport or dispose of the most dangerous substances, which are kept track of and often have to be treated before incineration or landfilling. These rules tend to be strictly enforced. Last month, for example, firms and municipalities that had dumped hazardous waste in a landfill in New Jersey, causing local groundwater to be contaminated, agreed to a legal settlement of almost $100m to cover past and future clean-up costs.

Modern landfills are forced to take elaborate precautions (see article for an example from a British town called Pitsea). At a recent hearing about the proposed expansion of a landfill on the coast of California, one questioner disputed a bureaucrat's claim that global warming would not cause sea levels to rise fast enough to affect the site. Another wondered whether the landfill was as earthquake-proof as its owners claimed. A third queried the location of the wells used to test for groundwater contamination. Several worried that the five-yearly reviews of all these precautions would not be tough enough. The application was eventually approved—but a decade had passed since it was first lodged.

Eyevine

In his book "The Economics of Waste", Richard Porter, an academic, examined the costs and benefits of the American government's decision to tighten controls on leachate from landfills in 1991, using data supplied by the Environmental Protection Agency (EPA). The EPA said its new rules would save 2.4 people from cancer over 300 years, at a cost, Mr Porter calculated, of $3.5 billion each. If the agency's standard discount rate is applied, the cost rises to $32 billion for each life saved. True, leachate can lead to many lesser health problems and environmental effects that the EPA did not assess. But the sums give a sense of how stringent landfill regulation in rich countries has become.

The same is true of the rules for incinerators. Indeed, their advocates now prefer to call them waste-to-energy or energy-from-waste plants, which sounds more positive. One of the world's biggest such plants, in

Fairfax County, Virginia, takes in about 1m tonnes of municipal waste a year, slightly more than the Pitsea landfill. Two sinister-looking six-taloned mechanical claws worthy of a Bond film grasp rubbish five tonnes at a time and drop it onto a conveyor. The moving metal grates carry the waste slowly through a furnace at ever-increasing temperatures to ensure a thorough burn. The plant generates up to 80MW, enough to power 75,000 homes.

In the control room technicians pore over second-by-second readings of the levels of different pollutants in the exhaust. To eliminate dioxins, regulations require that the waste reach a temperature of at least 1,800°F. In the smokestack, different filters remove oxides of sulphur and nitrogen, acidic gases, heavy metals and soot. All the water used goes through its own treatment plant. The ash is moved straight to an adjacent landfill, where it takes up only a tenth of the volume of the original waste.

Hulking hazards

Burnt offerings

The EPA has calculated that such controls have reduced emissions of dioxins and furans from America's incinerators from 8,900 grams a year to 80. By contrast, burning of household and garden waste in barrels and bonfires produces 500 grams a year. Germany's environment ministry reckons that incinerators have actually helped to improve air quality by reducing the need for dirtier coal-fired power plants. Yet local authorities in many countries remain hostile to new incinerators. No new ones have been built in America, for example, since 1995.

It would be reckless to claim that stricter controls have solved all the West's waste problems. Much still remains to be cleared up from the time before the new rules were adopted. And no regulations are foolproof. Environmental groups such as Greenpeace argue that landfill gas systems capture a lower proportion of methane emissions than waste firms claim, and that the liners that keep leachate in landfills are bound to spring leaks sooner or later. The regulators who say that burning rubbish is now safe were making the same claim when incinerators were still spewing out dioxins. And anything that is burned rather than recycled represents an energy loss, since more power will be needed to produce replacement materials from scratch.

On the whole, however, landfills and incinerators seem to attract a disproportionate amount of scrutiny and regulation—especially given that some equally dangerous facilities are barely monitored at all. A worrying loophole in America's rules was revealed in December of last year when a collapsed dyke sent a billion gallons of toxic sludge pouring into 300 acres of rural Tennessee. The sludge, a mixture of water and ash from a coal-fired power plant, contained significant amounts of poisonous heavy metals. Officials say the local drinking water is still safe, although the spill has killed fish in nearby rivers. The utility concerned, the Tennessee Valley Authority, says it is spending $1m a day on the clean-up.

That coal-ash pond in Tennessee is just one of about 1,300 similar repositories across America. The EPA believes that lax disposal of coal ash has led to the contamination of groundwater in 24 states. But under pressure from utilities it had previously dropped plans to classify coal ash as hazardous waste. Last month Lisa Jackson, the agency's new boss, promised in her confirmation hearing to return to the subject.

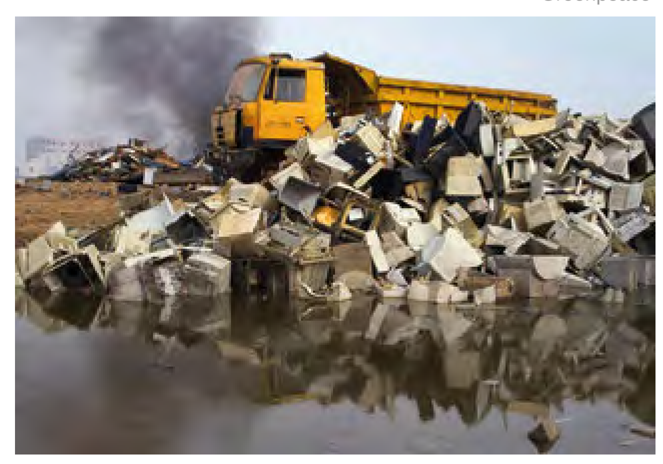
In poor countries waste is still much less strictly regulated, and the few rules are seldom enforced. In Madagascar, for example, only 6% of the rubbish is collected at all. Other countries manage to gather their waste, but do not supervise its disposal. The biggest landfill in Mumbai, India, called Deonar dumping ground, is just that. Opened in 1927, it occupies the same area as Pitsea but takes in almost twice as much waste a year. Goats and buffaloes graze amid the reeking mounds, and thousands of scavengers comb the site, looking for items of value. When trucks arrive to dump their loads, these "rag-pickers" surge forward to get first choice of the refuse. The ensuing mêlées often lead to injuries, says Prakash Tawase, Deonar's manager.

Hold your nose

Mr Tawase has no budget for fencing or crowd control, let alone modern environmental safeguards. No

attempt is made to control leachate, which swills out into the surrounding creeks and marshes and on into the Arabian Sea. He does not know how dangerous it is, because the water is not tested. Nor is there any system to collect landfill gas. So during the dry season several fires break out every day and smoulder away, releasing plumes of acrid smoke. Mr Tawase's staff try to fight these with a water truck and hoses.

Greenpeace



Not as clean as it looks

Local residents complain that the dump gives off horrible smells and that the smoke from the fires causes asthma and other respiratory ailments. They regularly lodge complaints and march in protest to the city council's offices. Last year some went on hunger strike. Local officials freely admit that the dump is a source of serious pollution.

Deonar is by no means unusual. Most of the developing world's waste, says Luis Diaz, of CalRecovery, a waste consultancy, is put into open dumps with no controls on leachate or landfill gas. Open burning of waste, another common disposal method, releases lots of dioxins, just as it did in incinerators in the rich world before the rules were tightened.

In 2007 the Blacksmith Institute, an American NGO, listed Dandora in Kenya, the site of Nairobi's main dump, among the world's 30 most polluted spots. Other places on the institute's list included La Oroya, Peru, where poorly managed effluent from 80 years of mining and smelting has left local children with three times more lead in their blood than the World Health Organisation's recommended maximum; and Dzerzhinsk, Russia, where 300,000 tonnes of chemical waste were disposed of haphazardly, mostly in Soviet times. Life expectancy in the city is 42 years for men and 47 for women.

Another big worry is the export of hazardous waste from rich countries, where it would be expensive to get rid of, to poor ones, where it can be dumped cheaply. In principle, under a treaty called the Basel Convention, this is illegal unless the receiving government has given explicit prior consent. But exporters sometimes succeed in passing off waste chemicals as useful ones, or clapped-out computers as donations for the poor. If ill-paid customs officials spot the deception, they can often be bribed to turn a blind eye.

The United Nations estimates that the world discards up to 50m tonnes of electronic goods, or e-waste, every year. Official recycling efforts in rich countries capture just a small fraction of this, according to Greenpeace. Most ends up in poor countries where scavengers break apart old mobile phones, computers and televisions to extract valuable metals for recycling, releasing various harmful substances in the process. In an area in Ghana where e-waste is stripped, Greenpeace recently found high levels of lead, dioxins and phthalates, which can damage the liver and testes. Similar degrees of contamination have been found at e-waste dumps in India and China.

Many poor countries have built thriving, officially sanctioned industries to recycle waste that would be considered hazardous in the rich world. Almost all the world's big ships, for example, are dismantled and recycled in India, Bangladesh and Pakistan. Shipbreaking provides jobs for tens of thousands of people, as well as cheap raw materials for industry. But slicing up huge oil tankers or freighters on beaches releases oil, heavy metals, dioxins, asbestos and other toxic chemicals into the sea.

Last voyage

The sea is the ultimate receptacle for much of the world’s waste. Rubbish is dumped into it by ships, or thrown or blown into it from coastal settlements, or washed into it through rivers, drains and sewage pipes. According to the United Nations Environment Programme (UNEP), perhaps 6.4m tonnes of waste finds its way into the sea each year. The Pacific “gyre” is the worst-affected area, but the problem is universal. Research suggests that every square kilometre of the ocean has an average of 13,000 pieces of plastic floating in it. And according to other studies, the floating portion makes up just 15% of “marine litter”; another 15% washes up on the shore and 70% ends up on the sea bed.

The plastic waste, in particular, does great harm to marine life. Birds, fish and other animals often die after becoming entangled in it or mistakenly eating it. It can smother reed beds, reefs and other important ecosystems. It can absorb toxins, making it more dangerous still to ingest. Even tiny barnacles take in microscopic fragments of the stuff, which then move up the food chain, with unknown consequences. The damage is not just to the environment but to fisheries and tourism too. Yet the world’s governments have made little effort to regulate marine waste at all.

A better hole

Feb 26th 2009
From The Economist print edition

The charms of modern landfills

LANDFILLS in rich countries have to jump through a lot of hoops to make themselves acceptable these days. For example, the facility at Pitsea in Britain, on the banks of the River Thames near London, accepts only solid municipal and commercial waste, because European law prohibits the mingling of liquid and solid waste, and of hazardous and non-hazardous waste. Its permit allows it to take in a million tonnes of waste a year. The plan requires the parts of the site facing a nearby road and houses to be filled in and rehabilitated first to help hide it from locals' eyes—even though just across the river a massive oil refinery looms.

The landfill sits on a natural foundation of London clay which is more or less impermeable. The owner, Veolia Environnement, one of the giants of the industry, has built an underground wall of similarly waterproof clay around the site which extends deep enough to reach the natural barrier below. The idea is to seal off the landfill from the surrounding marshes and river, preventing any contaminated water—"leachate" in the industry jargon—from leaking out. Landfills without the benefit of a naturally impermeable layer use plastic liners and imported clay.

A system of ditches and drains collects all the leachate, which is pumped through a treatment plant similar to a sewage works. Before it can be released back into the nearby watercourses it has to meet stringent standards, including maximum levels of ammonia, heavy metals and any chemicals that might cause oxygen depletion. Veolia is required to sample water from the surrounding area regularly.

The firm also has to collect the methane emitted by the landfill, which has meant sinking 1,000 wells at regular intervals across the 120-hectare site. The gas fuels ten turbines, each of which generates 14MW of electricity. Air quality, dust, litter, odours and vermin are strictly controlled too. At other sites Veolia has to use falcons, cannons, scarecrows, sonar and other gadgets to scare off the birds that try to scavenge on the rubbish, but not at Pitsea, because the surrounding wetlands are among Britain's few remaining breeding grounds of the black-tailed godwit.

From here to eternity

Veolia must also set aside money to ensure that the leachate continues to be treated, the gas collected, the local environment monitored and any damage remedied after the landfill stops accepting waste, which is meant to happen in 2015. Funding for these financial guarantees makes up 10-15% of the tipping fee of around £25 a tonne (not including the government's landfill tax). The firm's liability lasts as long as the landfill continues to generate leachate or gas. All the data on pollutants are published. Visitors are always amazed, the site manager says, to discover how much more there is to landfilling than tipping waste in a hole.

The appliance of science

Feb 26th 2009
From The Economist print edition

Trash goes high-tech

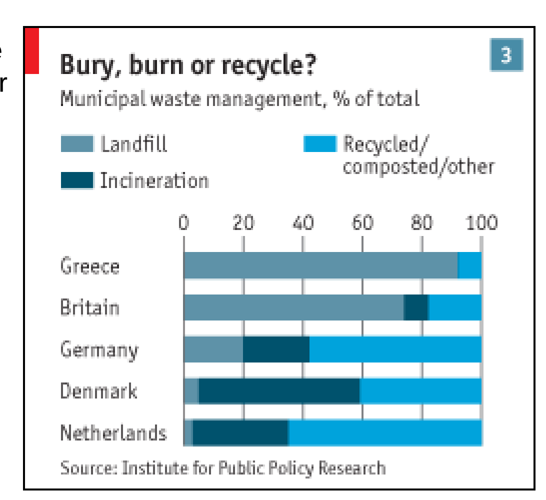
CAN a landfill ever be too sanitary? Perhaps surprisingly, the answer is yes. Some of them, it turns out, are so dry and airtight that their contents never rot. During its excavations of different landfills, the Garbage Project at the University of Arizona has encountered 15-year-old steak, with fat and meat intact, and 30-year-old newspapers, still quite legible. It concluded that in many landfills only food and garden clippings rot. Other supposedly biodegradable materials, such as paper and wood, often do not decompose at all.

That may sound like a good thing because it reduces methane emissions and leachate. But it also spreads out the risk of pollution over a very long period. And methane is difficult to capture in small volumes at low concentrations. So Waste Management, America's biggest waste firm, has been experimenting with a type of landfill called a "bioreactor", designed to ensure and accelerate the decay of biodegradable waste by injecting a mixture of air, water and recycled leachate. That should increase not just the amount of methane collected but also the capacity of the landfill, since waste shrinks as it rots. It should also reduce the degree of monitoring and treatment needed after closure, and allow the site to be put to another use more quickly.

Waste Management has tried pumping different mixtures through landfills to achieve the desired effect, and found that injections of out-of-date beer and soft drinks work better than water. It has managed to produce gas four times faster than normal and reduce the volume of the waste by up to 35%. The firm has already applied the technique to six landfills and plans to add more this year and next.

Burying is not the only form of waste disposal where new techniques are being tested: burning and recycling, which in some countries account for a large proportion of the total (see chart 3), are also going through great technological upheaval. The next section of this report (see article) looks at recycling in the traditional sense, of salvaging used metal, plastic and paper. But the sort of recycling where the kit is changing fastest is arguably the humblest: composting. Converting waste into fertiliser saves space in landfills and provides an extra source of revenue. But traditional composting does not save as many greenhouse-gas emissions as it might, since it still involves decomposition.

Hence the recent enthusiasm for a technique called anaerobic digestion, which extracts energy and fertiliser from biodegradable waste while also reducing emissions. Animal slurry, food scraps or garden clippings are placed in vessels that capture the methane as they decompose, leaving nothing but liquid and solid fertiliser—which add to the emissions savings by taking the place of chemical fertilisers made from fossil fuels.



However, even small amounts of stray plastic or glass can cause the whole process to break down. Municipalities that ask residents to separate their biodegradable waste from other rubbish often end up with material that is too contaminated to be of much use. It is only in places with lots of farms generating big quantities of animal slurry, such as Denmark and southern America, that the practice is taking off.

Another nascent treatment for biodegradable waste is enzymatic hydrolysis, which uses enzymes to break down complex molecules into sugars from which ethanol can be fermented. At present this process is uneconomic, but Steen Riisgaard, the boss of Novozymes, one of the firms that make the enzymes, says the cost is falling fast and claims that his American customers will be making money by 2011, with the help of government subsidies.

If Mr Riisgaard is right, there is a wealth of farm waste that could be turned into fuel, from corn cobs to citrus peel to wood chips. By 2030, America aims to produce 5% of its power, 20% of its transport fuel

and 25% of its chemicals from biomass—mostly farm, forestry and municipal waste. By the same date the European Union estimates that waste could provide about 6% of all its energy.

It is burning, however, that has attracted the most futuristic technologies. In many countries waste-to-energy technology in its traditional form is being held back by fears about pollution, which make it hard to get licences and permits. Moreover, waste can vary enormously from place to place and day to day, making it hard to calibrate equipment. That can lead to higher maintenance costs and lower energy yields than expected.

One solution is to treat waste before burning it to obtain a more consistent fuel. The simplest technique is to chop it up. That helps a little, but does nothing to separate out the items that do not burn or that would fetch a higher price if recycled.

Sterile solution

Instead, several firms are touting an alternative treatment called autoclaving. In essence, autoclaves are industrial-sized rotating pressure-cookers. They have been used to sterilise things since the 19th century, but steaming municipal waste in them is a new idea. The combination of heat, motion and pressure cleans recyclable items, even washing off labels and glue. It also breaks down food, paper and other combustible material into a fibrous mass that can be used either as fuel or for anaerobic digestion. The fuel is of sufficient quality and consistency to allow it to be used as a substitute for coal in factories and power plants, not just in incinerators.

A British firm called Sterecycle opened the world's first big waste autoclave in north-east England last year and recently announced plans to double its capacity. A rival, Graphite Resources, is building an even bigger plant nearby and there are plans for several more around Britain. But industry veterans question whether the revenue from the recyclables and the fuel will justify the capital and running costs.

Much the same doubt surrounds two other technologies called gasification and pyrolysis. Again, both have been around since the 19th century, but used for other things. They both involve heating, rather than burning, waste until it breaks down into a flammable mixture of carbon monoxide and hydrogen, called syngas, and residual char, ash or slag. The syngas can be converted into a number of different chemicals or even liquid fuel. Waste Management, for example, has started a pilot scheme to turn it into diesel.

A few dozen gasification and pyrolysis plants are up and running in Europe and Japan, and more are planned. Proponents argue that they are cleaner than existing waste-to-energy facilities. But the main advantage of these technologies over incineration, at least in theory, is that syngas can power gas turbines to make electricity. These are more efficient than the steam turbines used in waste-to-energy plants. The hitch is that syngas from waste is full of tarry residue that tends to gum up the turbine. It usually needs to be filtered, a step that raises the cost and reduces the overall efficiency of the process.

Several firms have come up with ways to make cleaner syngas. One method involves a device called a plasma arc gasifier, which generates artificial lightning bolts between two electrodes. The temperature of the arc itself can reach 13,000°C or more. Even a few feet away it can be over 4,000°C, more than enough to vaporise most waste and break down complex molecules. When the gas is cooled, any hazardous elements in the waste end up sealed in a glassy slag that is safe to put into landfill.

What some pilot plants have shown so far, however, is that a lot of the electricity produced is needed to power the arc. Plans for the first full-scale facility, in Saint Lucie, Florida, were recently scaled back.

Ze-Gen, based in Massachusetts, gasifies waste by injecting it into molten steel. The syngas rises through the pool, heavy metals sink to the bottom and other contaminants form a slag on top. Running this kind of furnace, says Bill Davis, the company's boss, consumes only 15% of the energy it produces.

The chief problem Ze-Gen and other firms with whizz-bang waste technologies face, says Mr Davis, is raising money to build full-scale plants. At the moment neither banks nor individual investors have the appetite to take a punt on an unproven idea. In the longer term he worries that so many new waste-processing facilities will spring up that they may actually have to compete for rubbish.

Round and round it goes

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From The Economist print edition

Recycling is good for the environment, but it costs. Is it worth it?

GREG RUIZ and Tara Bai Hiyale live on opposite sides of the world, in utterly different cities: San Francisco and Mumbai. Mr Ruiz has a steady job which brings in almost $20 an hour, along with a pension, health insurance and even a stake in the company concerned, thanks to an employee share-ownership plan. Mrs Hiyale lives hand to mouth, subsisting in a slum on 100 rupees a day with the help of a local charity. Yet they both do the same job: sorting through the local rubbish, trying to salvage goods that can be re-used. The stark differences in their circumstances say a lot about the global business of recycling.

In India, recycling provides a livelihood for millions. Most urban households do not throw out unwanted paper, plastic and metal. Instead, they save it and sell it to itinerant traders called *kabari-wallahs* who come to call at regular intervals. The remaining waste is picked over by the cleaners and watchmen at the apartment block they live in before being put out in a municipal skip where rag-pickers like Mrs Hiyale search through it again. When trucks deliver the rubbish from these skips to dumps such as Deonar, more rag-pickers comb over it yet again.

Mumbai is thought to be home to hundreds of thousands of rag-pickers. No wonder that until recently Mrs Hiyale could not count on a steady income. What she earned depended on how much she found scouring the streets and rummaging through the skips of the suburb of Ghatkopar, where she lives, and the price her discoveries fetched. Most of the time she took in less than 100 rupees a day. She had become a rag-picker decades ago when a drought struck Mumbai's rural hinterland, forcing her and her husband to abandon the land they farmed and seek work in the city. "Every day was a bad day," she says.

A few years ago Mrs Hiyale came across Stree Mukti Sanghatana, a feminist charity that seeks to provide female rag-pickers (the vast majority) with more stability and security. Now she retrieves the rubbish of apartment blocks that have an arrangement with the charity and sorts the recyclable portion in one of its sheds. She still earns only 100 rupees a day, but at least, she says, she has access to a steady stream of waste. She also has somewhere to store the material she collects, safe from thieves and gouging policemen. And she no longer has to work outdoors all day in the blazing sun and torrential monsoon rain.

The swarming flies and sickly, fetid smell that fill the shed do not seem to put her off her work. She sits on a low, pink plastic stool, behind a mound of unsorted goods which she is gradually dividing into smaller piles. Copper wiring goes in one heap, aluminium foil in another. Iron and steel is divided by thickness; the heftier pieces fetch a higher price. The same goes for plastic bags. Cloth, leather, Tetra Paks—each has its own pile. Coconut shells go into a bag hanging from the rafters.

Another woman comes in, carrying a load of plastic bottles several times her own size on her head. She will sort it by type of plastic and by colour. In another part of the shed a third woman stands knee-deep in waste paper which she is separating into cardboard, newspaper, office paper, glossy paper, coloured paper and envelopes—which, she says proudly, fetch four rupees a kilo, against just one rupee for the newspaper.

Rag-picking de luxe

In San Francisco, Mr Ruiz works for Norcal Waste Systems, which handles most of the city's household rubbish. Some days he stands by a conveyor belt in a huge warehouse, picking wood, cardboard, plasterboard and metal out of demolition debris. The belt moves quite fast, so only the biggest pieces can be retrieved. The rest falls into a skip, to be hauled off to a landfill.

At other times he drives a bulldozer in "the pit", where rubbish trucks dump San Francisco's household

waste, to be loaded onto bigger trucks also headed for the landfill. In theory, residents have already separated out anything that is recyclable or biodegradable. In practice, many do not bother. Lots of plastic bottles and paper can be seen through the muddle and grime. A study commissioned by Norcal found that 70% of the material going into the pit could have been recycled.

In another cathedral-like warehouse by municipal Pier 96, Norcal sorts the stuff local residents put into their recycling bins. An impossibly complicated network of conveyor belts, chutes and tubes whizzes the trash this way and that. Machines separate out different materials, in much the same way as Mrs Hiyale and her fellow rag-pickers do back in Mumbai. A magnet lifts up any iron and steel. A gadget called an “eddy-current separator” causes other metals, such as aluminium and copper, to jump, literally, off the line into different bins. A series of whirling discs arranged into a steep slope carries the lighter goods—mainly paper—upwards but allows heavier ones to fall. Workers pick off phone books, glass and plastic bottles.

Yet despite all this clever kit, the sorting at Pier 96 is much less elaborate and precise than that performed by Mumbai’s rag-pickers. Plastic and paper is separated into fewer colours and categories; indeed, many types of plastic are not accepted at all. The conveyor belts move too fast to catch everything and the workers and machines both make mistakes that they cannot correct.

PANOS



It’s a job

Norcal is constantly striving to recycle more, and to improve the purity of the processed waste it produces. As it is, the city of San Francisco keeps some 70% of its waste out of landfills—one of the highest rates in the world. That figure is all the more remarkable because almost none of the non-landfill waste is burned. The city council has set a goal of 75% recycling by next year and hopes eventually to achieve “zero waste”. It has written Norcal’s contract in such a way that the more the firm recycles, the more money it earns.

So Norcal invests in expensive facilities such as the one at Pier 96. It runs vigorous campaigns encouraging its customers to recycle. Its garbage trucks are covered with big pictures contrasting mouldering cardboard with healthy forests and festering table scraps with prospering farms. It inspects its trucks to see which buildings or neighbourhoods are throwing away lots of recyclables and gets its staff to contact the worst offenders to urge them to be more careful. It even has an artist-in-residence programme, designed to show how useful and beautiful junk can be. A recent incumbent made a dress out of used plastic bags; another tried to express “our society’s abusive pattern of production and waste” by weaving bits of trash together.

No one knows Mumbai’s recycling rate, but it seems likely to exceed San Francisco’s, for a simple reason. In Mumbai recycling is a profitable pursuit for all involved, whereas in San Francisco it costs most residents money. Indian rag-pickers require no wages, equipment or electricity. By contrast, Norcal has invested $38m in the materials recovery facility (or MRF, in the industry jargon) at Pier 96 and keeps paying out on running costs.

The revenue from Norcal’s MRFs covers roughly half their outgoings. Metal is the only material that is consistently profitable to salvage, says Mike Sangiacomo, Norcal’s boss. Cardboard usually is; most of the other goods the firm sends for recycling, including glass, plastic and other types of paper, usually are not.

The shortfall is covered by Norcal’s customers, who pay about $25 a month for waste disposal. Whether that price is worth paying is a complicated question. The answer depends, among other things, on the cost of alternative disposal methods and the value ascribed to the environmental benefits. At the most basic level, recycling competes with landfilling. That is reasonably cheap around San Francisco.

However, Jared Blumenfeld, head of the city’s Department of the Environment, explains that even in California, with its strict regulation, landfilling involves environmental costs that the city wants to avoid on principle. Climate change is the biggest concern. California has adopted ambitious targets for reducing emissions, and methane from landfills makes up 18% of the city’s emissions.

There has been little detailed cost-benefit analysis of California's emissions targets, Mr Blumenfeld happily concedes, or of San Francisco's aim of zero waste, or of any of the myriad environmental targets set by the city and by the state. Politicians adopt them because they think voters will like the sound of them. And they do: the recycling programme, Mr Blumenfeld says, is even more popular than the mayor, Gavin Newsom, who won 72% of the vote at the most recent election.

But there must be a price that even San Franciscans would balk at paying to reduce their waste. Mr Sangiacomo thinks he could increase the recycling rate by getting the trash in the pit sorted manually, but is not sure the city council would approve the extra expense. In less high-minded places, voters and politicians may well snap their purses shut much sooner.

That is what governments all around the rich world are now grappling with. The economic downturn has cut prices for recyclables by half or more since last summer. The shares of big recycling firms, such as China's Nine Dragons Paper, have plunged over the past year. The American and Canadian arm of Smurfit-Stone, which makes recycled cardboard, has filed for bankruptcy. Some traders have been reduced to stockpiling their wares in the hope that prices will rise. Others are asking governments for support.

There is little doubt that recycling is good for the environment. In 2006 the Technical University of Denmark conducted a review of 272 studies comparing the effects of recycling with those of landfilling or incineration. They came up with 188 scenarios involving different materials and recycling methods. In 83% of these scenarios recycling proved the greener of the available options.

For materials such as aluminium, the case is overwhelming. Recycling it requires only a tiny fraction of the energy consumed when mining bauxite and refining it into the same amount of metal. For other products the benefits are more finely balanced. Glass is heavy, so transporting it uses up a lot of fossil fuel. Collecting it and grinding it up into aggregate to make roads can consume more energy than taking it to landfill. But recycling it to make more bottles generally reaps an energy saving.

The green green glass of home

To recycle glass back into bottles, however, it needs to be sorted by colour. In general, the narrower the categories into which recyclables are sorted and the more meticulous the separation, the easier they are to process and the higher the price they fetch. White office paper is worth more than mixed paper, for example, and bottles made from a single kind of plastic are worth more than an assortment.

That is where the economics start getting tricky. Manual sorting is expensive in the rich world, which is why recyclables are often shipped to places with low labour costs. It helps that there are lots of almost empty container ships sailing back to Asia after unloading consumer goods in Europe and America: they will usually carry secondhand paper and plastic for a song. After preliminary sorting at Pier 96, for example, many of San Francisco's salvaged materials are loaded straight into containers bound for China, where they will be combed over much more thoroughly before being recycled.

The biggest American exporter by volume is a firm called American Chung Nam. In 2007 it sent off 211,300 containers of waste paper for recycling, almost all of them to its sister company in China, Nine Dragons Paper. There were six other recycling firms among the 20 biggest exporters. In 2006 CyclOpe estimated the value of the international trade in recyclables at well over $100 billion.

Sort it yourself

Another way to make recycling cheaper is to get the household or business that generates the waste to sort it free of charge. This is done without demur in much of Europe and Asia, where municipalities often collect paper, plastics, metal and glass separately. (Consumers can be further encouraged to return cans or bottles by including a deposit in their price.) But the Anglo-Saxon world dislikes sorting its own waste and often makes a hash of it. In San Francisco Mr Newsom wants to oblige residents to keep organic waste out of their rubbish bins. Originally he proposed fines of up to $1,000 for persistent offenders, but this caused such outrage that the figure was reduced to $100. Even so, says Mr Blumenfeld, the policy is unlikely to be vigorously enforced.

Retna UK



From bottle to bottle

Most cities in America are allowing their citizens to throw anything recyclable into a single bin, to be sorted out at an MRF like the one at Pier 96 in San Francisco. Thanks in part to the spread of such programmes, America's recycling rate doubled between 1995 and 2005, to 32%. Over the same period Europe's, which started at 22%, rose to 41%.

MRFs are getting more sophisticated all the time. At a plant on the outskirts of London a firm called Closed Loop Recycling sorts plastic bottles before recycling them. One machine uses optical scanning to work out what sort of plastic the bottles are made of. Blasts of air from a line of nozzles then direct each one to the appropriate bin. This device can cope with only a few different categories and often makes mistakes. But another machine in the plant, which uses a laser to scan the passing material, can sort plastic by type and colour with great accuracy.

This process, says Chris Dow, Closed Loop's managing director, was "a lab trial" two years ago. The firm is now taking part in a new trial to see whether similar devices can separate mixed plastics of all kinds rather than just bottles. That would dramatically improve the economics of recycling items of marginal value, such as yogurt pots. Thanks to such advances, says Mr Dow, the number of things that can be profitably recycled will keep expanding.

But Closed Loop can afford such fancy kit only because there is a strong market for its product: plastic of sufficient quality to be used to package food. British retailers are keen to increase the amount of recycled material in their packaging, partly because it is slightly cheaper than the virgin sort but mainly because their customers are keen on the idea. Tesco, Britain's biggest retailer, advertises a line of school uniforms made from recycled polyester. One of the ways it has responded to the growing clamour against plastic bags, says Alasdair James, its director of recycling, waste and packaging, is to use recycled ones.

Most of the bottles Closed Loop is currently recycling would otherwise have been shipped to China to be transformed into lower-grade plastic for cheap hard hats, artificial fleeces and the like. But such "downcycling" tends to be much less profitable than genuine recycling, and much more vulnerable to price swings. Closed Loop is still making money. It plans to build a second plant this year, despite the economic gloom.

Closed Loop's success did not come about by chance. The Waste and Resources Action Programme (WRAP), a government-funded agency charged with reducing landfilling, among other worthy goals, helped to pay for the initial trial of the recycled bottles. It also helped to bring together Closed Loop, Veolia (which supplies the used bottles), the retailers that buy the recycled plastic and the banks that financed the plant. It is now providing similar help with the attempt to sort mixed plastics.

WRAP's aim is to harness market forces rather than fight them. By getting municipalities and waste firms together it can ensure big and steady enough streams of different materials to justify investment in new recycling plants. By pooling potential buyers of recycled goods it helps to provide those plants with sufficient customers. And its involvement helps to reassure the investors.

But the most effective policy would be to incorporate the costs of the pollution caused by gathering and processing virgin materials into their prices. That would align environmental goals with business ones, sparing governments the trouble of trying to balance the recyclers' books.

 SPECIAL REPORTS

Muck and brass

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The waste business smells of money

RECYCLING aside, waste firms often describe themselves as recession-proof. The logic is simple: their workload is always increasing. As countries get richer and more urban and their populations expand, they throw away ever more stuff. The OECD forecasts that although municipal waste in rich countries will grow only by a fairly sedate average of 1.3% a year up to 2030, or about 38% in all, India's city-dwellers will be generating 130% more rubbish and China's over 200% more over the same period. That increase will come partly from a growing amount of waste generated per person but mainly from a rising urban population. Overall, Nickolas Themelis of Columbia University expects worldwide waste to double by 2030.

Growing wealth generally goes hand in hand with more concern for the local environment. In time, governments in developing countries will make sure that more waste is collected and tighten the rules about disposal. For example, India's Supreme Court has ruled that all cities of 100,000 people or more should provide a waste-collection service. The Indian government, for its part, has set guidelines and targets for treatment and is working on a law on e-waste. At present these rules are observed mainly in the breach, but with time and public pressure compliance should grow.

In rich and poor countries alike the authorities are increasingly inclined to entrust waste management to the private sector. That reflects not just the economic orthodoxy of recent decades but also the rising cost of complying with ever stricter environmental rules. In Britain municipalities have been obliged to hold public tenders for waste management since 1989. In America private firms dispose of roughly 70% of all waste. The more go-ahead cities in China, including Beijing, Shanghai and Guangzhou, have handed some rubbish-disposal contracts to private firms.

Mumbai offers a good example of the way things are going. Its collection rate is already well above the Indian average of 60%. Its environmental standards are also rising. Although almost all its waste currently goes to municipally owned dumps such as Deonar, with almost no pollution controls, the city plans to transform them into sanitary landfills and to build a new, greener facility from scratch. It is also installing equipment to collect methane and leachate at a recently closed dump, Gorai. The role of the private sector is growing: the local government has brought in consultants for the Gorai project and hopes to involve private partners in the landfill schemes. It is already using contractors to take most waste to its dumps.

One big Indian city, Chennai, has contracted out its rubbish collection to Veolia Environnement, one of the giants of the waste industry, which has a number of contracts in developing countries, including Brazil, South Africa and China. Its main rival, Suez Environnement, is active in China, Morocco and elsewhere. Covanta, the world's biggest waste-to-energy firm, already runs one facility in China and has several more in the works.

Alamy

Waste firms see ample opportunities in the rich world, too, because ever stricter regulations are helping to make up for the slower growth in waste volumes. On the whole, says Henri Proglio, the boss of Veolia Environnement, the more complicated the treatment, the higher the margin.

Between 1985 and 2005, as America's regulations got tighter and small landfills went out of business, average tipping fees rose from less than $10 per tonne to almost $35. But the European Union is probably the most zealous regulator: it has separate legally binding "directives" on waste policy in general, hazardous waste, the transportation of waste, pollution control, landfills, incinerators, and a host of specific sorts of waste, from cars to packaging to electronic goods. That has helped to push average tipping fees much higher than America's: €74 a tonne in France, for example,

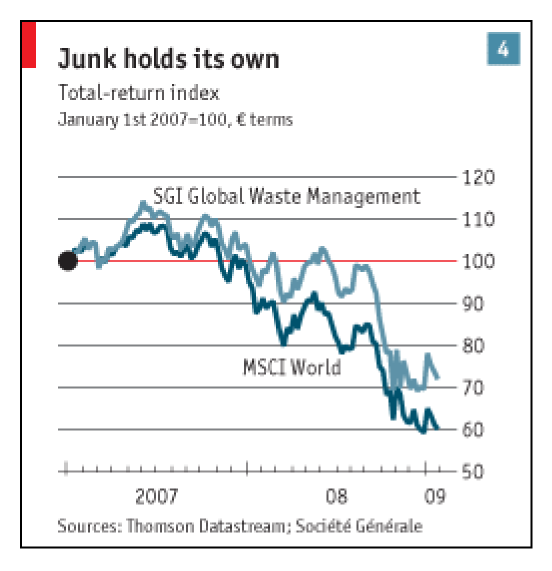
and €50 in Italy, according to CyclOpe.


Artful Spittelau

The big waste-industry companies welcome tighter regulation. Unlike the tiddlers, they can afford the investment needed to comply with it. The search for economies of scale has led to dramatic consolidation in recent decades. In Britain, between 1992 and 2001 the market share of the 15 biggest companies rose from 30% to 60%. In America consolidation is still in progress. Last year the third-biggest waste firm, Republic Services, spurned an offer from the biggest, Waste Management, and instead spent $6 billion buying the second-biggest, Allied Waste Industries. The two remaining firms have a combined market share of 41%, according to Standard & Poor's, a rating agency.

It just keeps coming

For such big, integrated firms, waste is also a very stable business. Although households and businesses produce somewhat less rubbish in tough economic times, the decline in volume is usually only a percentage point or two, says Mr Parker of the National Solid Wastes Management Association. And contracts often run for long periods. Four Winds Capital Management, an investment firm that is setting up a waste-industry fund, reckons that the average length of a collection contract is seven years; of a disposal contract, nine years; and of an integrated contract, 17 years. No wonder that the big firms' earnings are still growing nicely. Shares of listed waste firms have also suffered less than most in the recent downturn (see chart 4).



Waste firms often have multiple revenue streams, which can also help them weather a downturn. A waste-to-energy firm, for example, earns "gate fees" for taking the waste in the first place, as well as payments for the power it generates and any metals it recovers from the ash. Recycling firms are the obvious exception, but even they deal in a variety of goods whose prices do not always move in lockstep.

Concern about global warming should provide a big boost for the waste business in the future. Methane from landfills accounts for only about 4% of greenhouse gases, but it can be dealt with relatively cheaply and easily. Recycling tends to consume less energy than making goods from scratch, which helps to curb emissions.

Cities are particularly keen to tackle landfill gas, says Mr Blumenfeld of San Francisco's Department of Environment, because it is one of the few sources of emissions over which they have jurisdiction. And in places that do not have much heavy industry it can make quite a large contribution to total emissions: in San Francisco its share is 18%.

In many countries power from landfill gas or waste-to-energy plants (like the one at Spittelau, outside Vienna, illustrated above) attracts subsidies of one kind or another because it saves emissions. In the developing world it can earn UN-backed carbon credits, which can be sold to governments or firms that must reduce their emissions under the Kyoto protocol. Mumbai, for one, plans to sell such credits when its landfill-gas project at Gorai comes on stream.

Firms such as Covanta see worries about climate change as a spur to waste-to-energy projects. Incineration could save up to a gigatonne of emissions if widely adopted, says Covanta's boss, Anthony Orlando. That is about one-seventh of the current global total. Already, the world's 700-odd waste-to-energy plants generate more power than all its wind turbines and solar panels put together.

Japan and Singapore burn more than 50% of their municipal waste. Burning is also popular in many European countries. China currently incinerates only 2% of its rubbish, but has set itself a goal of 30% by

2030. That will involve an investment of at least $6.3 billion, according to New Energy Finance, a research outfit. Even America is thinking again: in 20-odd states that require utilities to generate a proportion of their power from renewable sources, waste-to-energy plants count towards the goal. Mr Themelis reckons it could supply as much as 4% of the country's electricity.

But it is Britain that currently offers the biggest incentives to waste firms. Trying to meet a target set by one of those European directives, it discourages landfilling by taxing it heavily. The tax rose by £8 per tonne in April last year, to £32 ($46, €37), and is set to rise by a further £8 both this year and next. In a country that still sends over half its waste to landfill, municipalities and businesses are desperate to find other ways of disposing of their rubbish.

No wonder, then, that so many of them are experimenting with avant-garde technologies. The government estimates that meeting the target will require £10 billion of investment. As one entrepreneur puts it, Britain is "beachfront property" for anyone with a nifty new waste-processing technology to sell.

Less is more

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The ultimate in waste disposal is to tackle the problem at source

SIEBEN LINDEN, a hamlet in former East Germany, half-way between Hamburg and Berlin, looks deceptively normal. There is a cluster of houses, some fields, a few cars parked by the side of the road and a small shop, all set against the backdrop of a looming pine forest.

Closer inspection, however, reveals a few peculiarities. Several of the modern-looking buildings turn out to be made of wood, straw and mud. There are huge quantities of logs, because wood-fired stoves and boilers provide all the heating, and quite a few solar panels, which generate most of the electricity. And there are more young people around than usual in rural Germany. Sieben Linden, a self-proclaimed eco-village, is growing fast, unlike the surrounding towns.

The 120 inhabitants have decided to live in as green a manner as possible. They are trying to wean themselves off fossil fuels, grow their own food and timber, acquire fewer frivolous possessions and produce less waste. Food comes either from their own fields or from wholesalers, so there is no need for much packaging. Any scraps are composted. Urine from the toilets is diverted to a reedbed for natural purification, and the faeces are turned into compost for the community's forest.

The residents live separately but share big appliances such as washing machines and cars. Before buying a new tool, say, they will put a note into the community's logbook to ask if anybody has one they could borrow. If not, they will probably buy one secondhand. They often wear one another's hand-me-downs. Unwanted possessions are left out for others to help themselves.

Carefree consumption is not actually forbidden, though it would raise eyebrows, says Eva Stützel, who helped to found Sieben Linden over a decade ago. But the main reason the inhabitants buy less and waste less is that they have a rich community life which does not revolve around trips to shops, restaurants and cinemas. They go ice-skating on a nearby pond in winter and swimming in summer; they teach one another horse-riding and yoga and tai chi; they put on plays and concerts and seminars.

The idea, explains Kosha Joubert, another resident, is not to adopt a dreary, ascetic lifestyle but to demonstrate that it is possible to live in a green manner without undue sacrifice or disruption. Western urbanites could easily adopt elements of the eco-village lifestyle, she says, by forming car pools, say, or shopping co-operatives.

Tipping point

Until recently most people in the waste industry had assumed that it was impossible to reduce the amount being produced and were concentrating on putting the stuff to better use. But lately that assumption has been challenged. For one thing, the pace at which the rich world churns out rubbish has been slowing.

Between 1980 and 2000 the amount of waste produced by the OECD countries increased by an average of 2.5% a year. Between 2000 to 2005 the average growth rate slowed to 0.9%. That was just ahead of the rate of population growth (0.7%), but well behind the rate of economic growth (2.2%). The OECD describes this as "a rather strong relative decoupling of municipal waste generation from economic growth", although it expresses some misgivings about the reliability of the data. The European Union has detected a similar trend in several European countries, as has CyclOpe, the research institute.

Reducing the amount of waste being produced makes a great deal of sense, provided it does not cost more, in either environmental or financial terms, than disposing of it in the usual way. Governments hope it might help to trim both greenhouse-gas emissions and waste-management costs. But they are not sure how best to encourage it.

Some are trying to persuade consumers to throw away less. The simplest method is to collect the rubbish less often. In areas of Britain where the dustmen come round only every other week, recycling rates are 10% higher than elsewhere.

Another tactic is to make households pay by volume for the rubbish they generate, rather than through a flat fee or through local taxes. Many places in Europe, America and Asia have adopted "pay-as-you-throw" schemes. (In Taiwan, householders even have to chuck their own rubbish into the truck.) About a quarter of Americans live in communities with such programmes. The EPA reckons that they reduce the volume of rubbish by 14-27% and increase recycling (which usually remains free) by 32-59%.

There are drawbacks. Fly-tipping—the illegal dumping of waste—tends to rise slightly as people try to avoid paying. And householders generally grumble a lot if they have to pay extra to have their rubbish collected. Some communities have responded by offering rebates to those who throw away less—a more palatable way of packaging the same idea. But most local authorities have simply decided against the idea. When the British government offered them money to experiment with pay-as-you-throw schemes earlier this year, not one signed up.

Businesses are generally seen as a softer target than consumers. It can be argued that manufacturers bear some responsibility for the amount of waste rich countries produce. They often have an incentive to reduce waste anyway, since most already pay for disposal by volume. There is even a name for the steady reduction in materials used to make the same goods: "lightweighting". It is not only electronic gadgets that have become smaller and lighter over the years even as their performance has improved but many other things too, from cars to plastic bags.

Sieben Linden



A lifestyle choice at Sieben Linden

The average aluminium drink can is now only half as thick as it was in the 1960s, according to Molson Coors, the firm that introduced this type of container in 1959. Its American subsidiary has reduced the weight of its cans by 7% in the past five years alone. That means savings not only on the metal itself but also on transport and even cooling: thinner cans chill faster.

Officials in the EU, in particular, are keen to hurry lightweighting along. WRAP, the British agency charged with reducing waste, is trying to promote it for various sorts of packaging. It funded trials of a lightweight pull-tab lid for food tins, which it believes could save 15,000 tonnes of steel each year in Britain alone. Heinz, a giant food manufacturer which took part in the trial, hopes that adopting the new lids will save it £400,000 a year. WRAP has conducted similar tests of thinner glass and plastic bottles, with equally promising results.

WRAP also cajoled Britain's biggest supermarkets and food suppliers into signing a voluntary agreement to halt the growth in packaging by last year and start reducing it from 2010. Last July it announced that the initial target had been met, despite a 1.8% rise in sales. Some firms are going much further: in 2007 Tesco pledged to reduce its packaging by a quarter by 2010.

In theory, consumers could steer firms towards waste reduction by buying products that are easy to recycle, say, or have only minimal packaging. To some extent this is happening. Tesco's Alasdair James says British consumers rank the environment as their third priority after price and convenience. But many governments are trying to give greenery an extra push with compulsory waste-reduction schemes.

Some levy fees on certain products, akin to bottle deposits, to ensure they are disposed of safely. Thirty-six states in America, for example, charge for the disposal of tyres. The states spend the money on clean-up programmes or pay others to run such programmes. Many of the tyres are blended into road surfaces or burned in cement kilns. Several other states have "advance recovery fees" for computer monitors and televisions. So have Japan, South Korea and Taiwan, among others, and China is working on a scheme.

The problem with fee programmes is that all goods in a category are subject to the same charge, whether they are easy or hard to get rid of. That gives manufacturers no incentive to build easy disposal into the design of a product.

One answer is to ban certain substances outright, thereby eliminating the need to dispose of them later. A number of places, from San Francisco to the tiny Himalayan kingdom of Bhutan, have banned or severely restricted the use of plastic bags. The EU barred the use of several heavy metals and flame retardants in electronic goods in 2006 and recently proposed expanding the scheme. Several American states were so impressed that they have copied the EU's rules.

Return to sender

But the EU has gone further, applying a concept called "extended producer responsibility" to an ever-expanding list of items including cars and computers. At its simplest, this means that manufacturers have to take back their products without charge when consumers have finished with them. The EU's directive on "end-of-life vehicles" not only obliges manufacturers to accept vehicles that are no longer wanted, but also requires them to recycle or re-use 80% of the parts by weight, a proportion that will rise to 85% by 2015. The manufacturers can farm out the job, but only to authorised firms.

Hewlett-Packard (HP), which makes lots of electronic devices that are subject to such rules, says it welcomes them. It has always tried to design its products not just from cradle to grave, a spokesman explains, but from cradle to cradle—meaning with recycling in mind. Its laptops are 90% recyclable and its printers at least 70%. By last year HP had recycled over 450,000 tonnes of used equipment. It aims to double that figure by the end of next year. At its facility in Roseville, California, workers first check discarded computers and printers to see if they can be re-used: it refurbishes 2.5m devices a year. The rest are taken to bits. First the big, accessible parts are removed, along with anything dangerous, and then heavy-duty shredders grind up the remainder into tiny pieces that can be sorted by standard recycling equipment.

An engineer explains how a decade of such work has taught HP how to make the process simpler and cheaper. It now uses screws instead of glues wherever possible, and has reduced the number of different kinds of plastic in its products from 200 to five. It plans to eliminate one more—polyvinyl chloride—from new computer models this year. It is proud of having closed the loop on ink cartridges for its printers, which it now makes from old cartridges.

But the firm would like to go further, designing computers so that they can be easily upgraded rather than replaced. Ultimately, says Chandrakant Patel, who heads its "sustainable IT ecosystems laboratory", modern computer systems will allow firms to calculate the precise disposal costs of a product during the design phase and include them in the sale price. More sophisticated products will also warn users when they are about to fail, eliminating the need for spare capacity.

Think before you legislate

Sadly, however, that sort of world is still a long way off. Governments are wildly inconsistent in their approach to extended producer responsibility. They tend to home in on particular products without justification (tyres, after all, are not among the biggest threats to the planet). Their goals seem arbitrary too: how did the EU decide that 85% of car parts had to be recycled, not 84% or 86%? And why should the deadline be 2015, not some other year?

Official thinking about waste in general seems equally confused. Why levy deposits to encourage the recycling of glass bottles but not plastic ones? Why control the disposal of municipal waste in such detail but allow utilities to pile up coal ash unchallenged? Why tax and regulate landfills out of all proportion to the damage they do to the environment? The individual policies do not add up to a grand design.

Alamy



It doesn’t have to be like this

A desire to reduce the amount of waste being produced and to minimise the harm it does is all well and good, but governments must be sure to encourage those ends by the cheapest and most efficient means. Plugging loopholes in the rules is a good first step. American officials should be much stricter about coal-ash tips, regardless of how much clout utilities have in Congress. Similarly, governments should pay more attention to waste that winds up in the sea, even if it falls outside their formal jurisdiction.

Emissions of greenhouse gases and other noxious chemicals are a worry. But instead of banning or heavily taxing particular waste-disposal technologies to reduce the emissions they produce, governments should tax or limit emissions in general. That would steer investors towards the cleanest technologies, whatever they might be. Thus, instead of clamping down on landfills because of the methane they produce, or incinerators for fear of dioxins, governments should tackle methane and dioxins across the board. If landfills and incinerators can meet the standards they set, they should be welcomed.

Putting a price on greenhouse-gas emissions would also help to promote recycling. At the moment, it is often cheaper to process virgin materials, despite the extra energy required, because collecting and sorting recyclables is so labour-intensive. Recycling produces far fewer greenhouse gases, but recycling firms do not get much benefit out of that because their rivals pay little or nothing for the emissions they produce. In effect, governments are subsidising the use of raw materials by failing to charge big energy users for the emissions they cause. Scrapping that subsidy would provide recycling firms with a big boost.

Above all, regulators should be conscious of the costs of the rules they lay down. Blanket bans, 100% targets and punitive taxes are usually a sign of dogmatism. It cannot be desirable for California to recycle absolutely everything. There must be some waste that is better burnt or buried. Construction and demolition, for example, produce lots of inert waste that can be cheaper to put into landfill than to “downcycle” into lower-value construction materials. And there is nothing wrong with burning wood or even some plastics, provided the right pollution controls are in place. Politicians should prize value for money above political correctness or rhetorical flourish.

Still, in their muddled and heavy-handed way, governments are groping towards the idea of making the polluter pay by internalising the cost of responsible waste disposal. That is surely the right way to go. If governments oblige manufacturers to include the cost of disposal in their prices, firms will pass those costs on to consumers, who will have an incentive to buy the products that are the easiest to dispose of and therefore cheapest. All this should provide a spur to the waste industry and speed the adoption of new technology. Firms like HP have seen the writing on the wall: waste is heading for a redesign.

Sources and acknowledgments

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Offer to readers

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Corporate planning

Managing in the fog

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From The Economist print edition

Illustration by David Simonds



The struggle to make meaningful forecasts in a downturn

"NOT to beat around the bush, but the budgeting process at most companies has to be the most ineffective practice in management." Thus Jack Welch, the former boss of GE, in his book "Winning", which was published several years ago. Many firms that put their 2009 budgets together at the end of last year will no doubt agree with him. Most of them will have already been consigned to the shredder, as the economic crisis has blown away the assumptions on which they were based.

Faced with exceptionally volatile business conditions, senior executives are finding it harder than ever to gauge how their companies are likely to fare in the months ahead. According to a recent global survey of 1,300 chief financial officers (CFOs) by Tilburg University in the Netherlands, America's Duke University and *CFO Europe* magazine, a sister title of *The Economist*, finance chiefs say that the struggle to produce accurate forecasts now tops the list of things that keep them awake at night.

With even short-term horizons as obscure as the San Francisco skyline during a summer fog, companies are finding their standard budgeting and forecasting of little use. The usual trick of plugging figures from operating units into spreadsheets appeals to number-crunchers, but can often generate misleading targets, especially when conditions change fast. "The annual budget is even less of a meaningful document this year than usual," argues Cynthia Jamison of Tatum, a consulting firm that also provides clients with interim CFOs.

What can companies do? A few forward-thinking firms can provide inspiration. Hugh Courtney, a professor at the University of Maryland's Robert H. Smith School of Business, thinks more companies should be using "scenario planning" alongside their financial models, which do not produce a large enough spread of possible outcomes to capture the flavour of today's uncertainties. Sten Daugaard, the finance chief of Lego, a Danish toymaker, says his firm generated a number of different scenarios as part of its 2009 budget, the first time it had used such an approach. It has developed contingency plans for each scenario so that it can react swiftly whatever the coming months throw at it.

Lego has also been using a monthly meeting of senior managers, known as the operations board, to pool knowledge of what is happening in its various markets. At each get-together, the firm's executives not only discuss what has been going on that month, but also make their best guess about what is likely to happen in the 12 months to come.

Some companies have formalised this kind of approach by creating "rolling forecasts". At the end of, say, the first quarter of a financial year, managers forecast the remaining three quarters again and then add an extra quarter's projections, worrying about only the most important financial variables. Many companies in Europe already use such systems, says Emery Sinclair of Revelwood, an American software-services provider, and firms in America are suddenly taking a lot more interest in them. One benefit of rolling forecasts is that they discourage executives from becoming too fixated on the present at the expense of the future.

In praise of short-termism

Yet with economies in free fall, managers also need up-to-date information about what is happening to their businesses, so that they can change course rapidly if necessary. Cisco, an American network-equipment giant, has invested over many years in the technology needed to generate such data. Frank Calderoni, the firm's CFO, says that every day its senior executives can track exactly what orders are coming in from sales teams around the world, and identify emerging trends in each region and market segment. And at the end of each month, the firm can get reliable financial results within four hours of closing its books. Most firms have to wait days or even weeks for such certainty.

Admittedly, Cisco's financial results have not made happy reading recently because, in common with many other large technology companies, it has seen demand for its products falter in the downturn. In early February it announced that its fiscal second-quarter revenues of $9.1 billion were 7.5% lower than the same period in 2008 and that its profit had fallen by 27%, to $1.5 billion.

In response to hard times, Cisco plans to cut $1 billion of costs this year by, among other things, harnessing its own video-conferencing and other communications technologies to reduce the amount its executives travel. It is also using these facilities to relay information from employees on the ground to its senior managers, and to get instructions from Cisco's leaders back out to its 67,000 staff. A rapid exchange of information and instructions is especially valuable if the company wants to alter course in stormy times.

If everybody in a company can rapidly grasp what they have to do and how it is changing, they are more likely to get the job done. But some firms are reluctant to share their goals with the wider world. Unilever, a big Anglo-Dutch consumer-goods group, has decided against issuing a 2009 financial forecast to investors, arguing that it is difficult to predict what is going to happen, given the parlous state of the world economy. "We're not just going to provide numbers for the sake of it," explains James Allison, the company's head of investor relations. Other companies that have decided not to provide annual earnings estimates for 2009 include Costco, a big American retailer, and Union Pacific, an American railway company.

Some firms, such as Intel, seem to have chosen to take things quarter by quarter. The giant chipmaker said in January that it would not issue an official forecast for the first quarter of 2009 after its fourth-quarter 2008 profit plunged by 90%. Several retail chains have also stopped providing monthly sales estimates because they cannot see what the future holds. Retailers, chipmakers and firms in many other industries may have a long wait before the economic fog finally lifts.

 BUSINESS

Prediction markets

An uncertain future

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A novel way of generating forecasts has yet to take off

NOT SO long ago, prediction markets were being tipped as a fantastic new way to forecast everything from the completion date of a vital project to a firm's annual sales. But although they have spread beyond early-adopting companies in the technology industry, they have still not become mainstream management tools. Even fervent advocates admit much remains to be done to convince sceptical managers of their value. "It's still a pretty evangelical business," says Leslie Fine of CrowdCast, one of the firms that provide trading platforms for companies keen to pool the collective wisdom of their employees.

Prediction markets work by giving people virtual trading accounts that allow them to buy and sell "shares" that correspond to a particular outcome. Shares in an outcome that is considered more likely to occur then trade at a higher price than those that represent a less likely outcome. This provides a way to tap into the tacit knowledge that exists in companies, especially ones that have many different divisions or offices.

Jupiter Images



The mists are clearing

Koch Industries, an American conglomerate in a range of businesses including chemicals, fertilisers and commodity trading, has been running prediction markets for the past nine months involving about 200 of its staff from different areas. The group, which has revenues of some $100 billion, has launched contracts on, among other things, the future prices of raw materials used in its chemicals division and the likelihood of bank nationalisations. Koch says the results so far have been pretty accurate compared to actual outcomes, but stresses that markets are complementary to other forecasting techniques, not a substitute for them.

A big hurdle facing managers using prediction markets is getting enough people to keep trading after the novelty has worn off. Many firms use gaming-style leader boards to encourage internal rivalry, or offer modest prizes to the most successful traders. Lloyds TSB, a bank, launched a market in which participants identify the best new ideas by trading in a currency called Bank Beanz, which can then be exchanged for cash—a scheme the bank's head of innovation calls "an exceptional motivator".

Another reason prediction markets flop is that employees cannot see how the results are used, so they lose interest. Wells Fargo, a big bank that has been running internal markets for over a year to identify ways to improve service to some corporate customers, says its most effective trials took place in areas where managers could do something with their findings, making staff feel that trading was worthwhile.

Bosses may also be wary of relying on the judgments of non-experts. Yet many pilot projects run so far have shown that junior staff can often be surprisingly good forecasters. Perhaps the best way to find out when prediction markets will finally take off is to ask your employees—using a prediction market.

 **BUSINESS**

European energy

Power games

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The final shape of the European energy market is emerging: an oligopoly

AFTER years of legal fights, hurt pride and face-saving compromises, the saga of Endesa, a Spanish utility, and Enel, an Italian energy giant, came to an end on February 20th. It had started when the Spanish government tried to engineer a merger of Endesa with another Spanish utility, Gas Natural, in an effort to create a national champion. The eventual outcome, however, is that Endesa is now owned by Enel, Italy's leading energy firm. One lesson is clear: attempts by politicians to create energy champions can have unexpected consequences, and can make the governments in question look foolish.

In 2005-06 Endesa fought off the Spanish government's clumsy attempt to merge it with Gas Natural. Sensing an opportunity, E.ON, a German energy giant, made a bid for Endesa in 2006. Spain did everything it could to fend off E.ON, prompting the European Commission to intervene. In the end Enel won Endesa by bringing in a Spanish partner, Acciona, to appease local feelings. Remarkably, Enel, which had bought 67% of Endesa's shares, allowed Acciona to keep voting control of the Spanish company. This compromise proved disastrous: the two firms fought over strategy and Endesa suffered from a lack of direction. This week Enel finally took proper control of Endesa by buying out Acciona's 25% stake for €11.1 billion ($14 billion).

The Spanish complain that, whereas the government privatised Endesa in 1997-98 with the aim of improving efficiency and reducing electricity prices, the firm has now fallen back into government hands—Enel is 31.2% owned by the Italian state. Xavier Vives of IESE Business School doubts whether there can be a fair market for corporate control when some European governments keep stakes in energy firms and others do not. The Spanish failed to create a national champion, with the result that another country's champion has become far more powerful in the European market. "The Spanish are justified in feeling miffed," says Dieter Helm, an energy economist at the University of Oxford.

Another issue is the separation or "unbundling" of energy-production and transmission. Some countries, such as Spain, the Netherlands and Britain, have gone further than others, such as France and Germany, in unbundling their energy companies. The unbundlers think it is unfair for vertically integrated firms with superior firepower to come in and snap up smaller, unbundled companies. Last October the European Commission inserted a new "level playing field" clause into its draft energy-liberalisation package, the final version of which will be adopted this year, to allow countries that have fully unbundled to block acquisitions by more vertically integrated companies. The European Union's energy commissioner, Andris Piebalgs, commented that the Spanish government could have used such a clause to justify blocking E.ON's bid for Endesa, though he added that the courts might not have accepted the argument (E.ON agreed to unbundle its transmission operations some time after it made its bid for Endesa).

There was another big European energy takeover this week. Vattenfall, the largest utility in the Nordic region, bought the production and supply unit of Nuon, a Dutch energy firm, for €8.5 billion. And there have been other recent deals. In January RWE, a German giant, agreed to buy another Dutch firm, Essent, for €9.3 billion. This month the Spanish government also waved through the merger of Gas Natural with Union Fenosa, which will create a smallish national champion. With these deals, analysts say, the consolidation among European energy firms triggered by the liberalisation of the industry is drawing to a close. Apart from Scottish and Southern and Centrica, two British firms, there are few targets left.

What will the result look like? After several years of frenetic mergers and acquisitions, Europe is dominated by a few cross-border giants, such as France's EDF, which is 85% owned by the French state, Germany's E.ON and RWE, and Enel. Some countries have powerful national champions; others, such as Spain and the Netherlands, do not. Competition within markets may be largely unaffected—from a national point of view, two foreign utilities buying Essent and Nuon is better than the two Dutch firms merging, as they planned to not long ago—but at a European level, consolidation and concentration may be pushing energy prices higher, analysts say. "We've got an oligopolist electricity and gas market which looks a lot like the oil market—not at all what was intended," says Mr Helm.

 BUSINESS

Telecoms in India

The hesitant auctioneer

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After years of delay, India launches 3G telephony—sort of

AFP



ONE drunk driver, 32 traffic violations and 15 miscellaneous offences. A daily tally of crimes in Cochin, a city in the Indian state of Kerala, appears on the mobile phone of Sanjay Vijayakumar, the young co-founder of MobME. His firm, which provides "value-added services" for mobile phones, has outfitted the Cochin police with camera-phones. Instead of describing crime-scenes to their control room over a walkie-talkie, the police can now snap a picture (stamped with date, time, and place) and send it over the airwaves. It takes just a few seconds to send a photograph over India's mobile networks. But Mr Vijayakumar dreams of his customers sending live video. For that, India needs third-generation (3G) networks.

Mr Vijayakumar jokes that in India, 3G has been "just around the corner" for over three years. But this month 3G services were formally launched by Bharat Sanchar Nigam Limited (BSNL), India's national carrier, after their introduction in parts of Delhi by Mahanagar Telephone Nigam Limited (MTNL), the state-owned carrier serving Mumbai and the capital. On February 22nd the chief minister of Tamil Nadu, which neighbours Kerala, made an inaugural BSNL video-call to India's telecoms minister, A. Raja.

The two state operators can now begin expanding their networks. But for everyone else, 3G remains just around the corner. The government has yet to release radio spectrum to private companies for 3G services. A spectrum auction originally scheduled for January 16th has been postponed twice. It may not now take place until the third quarter of this year.

The ostensible reason for the delay is a row between the department of telecommunications and the finance ministry, which wants to raise the minimum price in the auction. The telecoms minister has an unfortunate reputation for surrendering the public airwaves cheaply, after allowing new entrants to buy 2G licences in January 2008 at a price unchanged since 2001. The scale of the undercharging became embarrassingly obvious last October, when two of the new licence-holders sold stakes to foreign operators prepared to pay handsomely for access to their spectrum. Norway's Telenor, for example, paid 62 billion rupees ($1 billion) for 60% of Unitech Wireless, which had no subscribers or network.

The government once hoped to raise about 400 billion rupees from the 3G auction. After the credit crunch, it now expects to raise only half that. But the fiscal proceeds from 3G matter less than the economic gains, according to Tom Phillips of the GSM Association, a telecoms lobby group. To put a number on those gains, his association commissioned a study by Leonard Waverman of LECG, an economics consultancy. He calculates that a five-year investment in 3G networks worth $15 billion in today's terms would yield a return to the economy worth more than twice that (over $35 billion). Accordingly, a year's delay costs $3.2 billion, because the benefits of 3G are deferred. Mr Vijayakumar laments "so many man-months wasted, just waiting for the uncertainty to unravel itself."

The government's hesitation may, however, suit some of India's telephone operators. Reliance Communications, having won over 60m 2G subscribers using one technological standard, has just crossed

over to the more popular GSM standard, dominated by its rivals Bharti Airtel and Vodafone Essar. Some analysts suggest that Reliance might prefer to wait until its GSM network has settled down before joining the battle for 3G customers. Reliance itself says it is ready to bid.

Whenever the auction is held, these rivals will lock horns, especially in Delhi, where only two slots are on offer. In some areas networks are horribly overloaded. By winning a 3G licence, companies can offer their most lucrative customers crisper calls, and also make room for the 9m 2G subscribers being added each month.

Kunal Bajaj of BDA Connect, a telecoms consultancy in Delhi, reckons that after five years India will have 60m 3G subscribers and another 29m using 3G networks through their laptops. Their combined spending will exceed $15 billion. In India, where fixed-line broadband links are rare, many will get their first taste of speedy surfing over a wireless network. They may see 3G handsets not as expensive phones, but as cheap computers, with which they can call up scores, prices and even crime reports. It’s just around the corner.


BUSINESS

Software in the recession

Out on its own

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Autonomy, Britain’s largest software firm, is prospering amid the gloom

LOSERS can sometimes land on their feet. After the internet bubble burst in 2000-01 Autonomy, a British software firm, had a dramatic fall from grace. Its share price dropped by more than 90%, as did the fortune of Michael Lynch, its founder, who had been hailed as Britain’s answer to Bill Gates. “No one needs a billion pounds,” he said, putting a brave face on it. As the technology industry shrinks once again, however, Autonomy is one of the winners. Today it is Britain’s biggest software company by market value, and there is no mistaking Mr Lynch’s satisfaction as he reviews his firm’s latest results. Revenues in the last three months of 2008, a disaster for most technology companies, were up 26% compared with the previous year, reaching $145m. Net profit more than doubled to $51m. What could explain this remarkable reversal of fortune?

For a start, the suffering of technology firms depends on how high up they are in the value chain. Chipmakers have been hardest hit so far, with some reporting revenues down a staggering 50%. Computer-makers are doing somewhat better, but deferring the purchase of new hardware is an easy way to cut costs. Many software firms, by contrast, have held up well—in particular, those that sell programs customers cannot do without, and that have stable revenue from licences and services.

Autonomy is a case in point. Many think of the firm, which Mr Lynch founded in 1996 with an impromptu loan from a drunken rock band manager in a London bar, as a kind of Google for corporate data. But its products do much more than just search for keywords in a company’s files. Using complex algorithms, they are able to extract ideas from all kinds of data, be it text, audio or video—even if these ideas are expressed in different terms.

From its inception, the software has been popular with government agencies, particularly intelligence services. But today 80% of Autonomy’s revenues come from companies. Demand here has been increasing rapidly, mainly because of growing regulatory burdens. In America, for instance, rules governing civil lawsuits now require firms to produce all relevant pieces of digital information in court. In the past, forking over the e-mail on a given topic was often enough.

In recent months, says Mr Lynch, big banks in particular have bulked up on Autonomy’s software, to prepare for lawsuits in the wake of the financial meltdown. He is betting that litigation will be an even juicier market in future: in January Autonomy bought Interwoven, an American maker of software that helps big law firms keep track of their documents, for $775m.

Yet the most important reason for Autonomy’s success is that it is riding a long-term trend in computing. Corporate computing was once all about “structured data” such as payroll records or sales figures. Now, however, computers are also able to crunch “unstructured” data, such as documents, e-mails and photographs. And the quantity of such data has exploded: more than 80% of a typical company’s information is now unstructured, according to some estimates. Firms that can extract meaning from this digital pile will have a big advantage.

Mr Lynch, who developed Autonomy’s technological underpinnings while writing a doctoral thesis at Cambridge University, wants his firm to become the “Oracle of unstructured data”, a reference to the database giant that is the world’s second-largest software firm. Autonomy seems well on its way to achieving that ambitious goal. A serious rival has yet to emerge, and some 400 other software companies have licensed the firm’s core technology, called IDOL, for their own products, so that it is fast becoming a de facto standard.

To be sure, Autonomy will have to compete against Microsoft, which has bought FAST, a Norwegian rival, says Madan Sheina of Ovum, a market-research firm. Autonomy could also end up being acquired, not least by Oracle, the industry’s big consolidator, which would certainly like to dominate the field of unstructured data as well. But for the time being, Autonomy is a rare bright spot in an otherwise

depressing high-tech landscape.

News Corporation

Home alone

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From The Economist print edition

The departure of Rupert Murdoch's second-in-command raises big questions

LIKE any good actor, Peter Chernin timed his exit perfectly. According to people close to him, he told Rupert Murdoch of his decision to leave his job at News Corporation some months ago, but the news came in the thick of the Oscar triumph of "Slumdog Millionaire", a small-budget film distributed by Fox Searchlight Pictures of which Mr Chernin is particularly proud. He had been widely expected to leave: nearly 13 years serving the Murdoch family as chief operating officer, with diminishing prospects of becoming chief executive, was evidently enough. He leaves with an unusually generous severance package and the right to sell at least two films a year to News Corp's Twentieth Century Fox.

For investors in News Corp, Mr Chernin's departure is worrying for several reasons. Could he see that things were about to get much harder for the company, making his job less enjoyable? Two decades ago, Mr Murdoch used the cashflow from newspapers to get into television and film. Now the pattern is reversed, with the businesses that Mr Chernin oversees in Los Angeles and elsewhere providing money to spend on print. Mr Chernin is believed to have disagreed with Mr Murdoch's decision to spend $5.7 billion on Dow Jones, the parent company of the *Wall Street Journal*, in 2007. Investors who are sceptical about investing further in newspapers may have lost an ally. His departure also raises the question of whether the firm's film and television assets will be as well-managed and profitable in future.

Bloomberg



Time to go, methinks

Mr Murdoch, who is almost 78, insists that he can do the number two's job as well as his own, which means accepting 16 direct reports from the company's senior executives. Even once he has streamlined that structure, notes Richard Greenfield of Pali Research, an independent research firm in New York, he will need to bring in a second-in-command.

Who that should be raises the question of succession, an issue that has long vexed investors. From Mr Murdoch's point of view, the obvious candidate is his youngest son, James, 36, who has run the company's European and Asian businesses well. At some point James was expected to move to America to gain experience of News Corp's businesses there. But James, it seems, will stay in his current job, despite the opening in Los Angeles. Ideally, Mr Chernin would have stuck around long enough to have shown James the ropes in America, ensuring a smooth handover. Now that transition looks likely to be rockier.

"Slumdog Millionaire", which was made for just $15m, might have gone straight to DVD in America had Fox Searchlight not spotted its potential, put it on cinema screens and reaped commercial as well as creative glory. Peter Rice, Fox Searchlight's boss, is one of the talented executives that News Corp insiders point to as evidence that the gap left by Mr Chernin will soon be filled. Nonetheless, investors may soon get the answer to an intriguing question: how much of News Corp's success in recent years was down to the mogul, and how much down to the professional manager?

Economist.com BUSINESS

Google in Asia

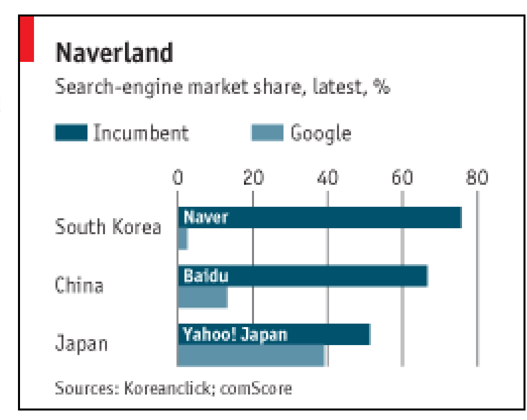
Seeking success

Feb 26th 2009 | SEONGNAM CITY AND SHANGHAI
From The Economist print edition

Google is not having much luck in South Korea, but it may be advancing in China

IN SOUTH KOREA people who want to look something up on the internet don't "Google it". Instead they "ask Naver". Among the 35m South Koreans who use the internet every day, the nine-year-old search engine is wildly popular, accounting for 76% of internet searches, compared with less than 3% each for Yahoo! and Google. Naver owes its popularity, in part, to the fact that it is not just a search engine. Like Yahoo!, it is also a portal, drawing together news, e-mail, discussion groups, stockmarket information, videos, restaurant reviews and so on. Some 17m people visit its home-page every day and since January they have been able to customise it according to their own tastes.

But Naver is also dominant—too dominant, say some—because it caters to the interests of South Koreans. "Yahoo! and Google have a very American, English-based search engine," says Chae Hwi-Young, the chief executive of NHN, Naver's parent company. If you go to Google and type in "rain", for example, the result is lots of pages about water falling from the sky. In South Korea, however, it makes more sense to return pages, as Naver does, about a popular singer and actor called Rain.



Naver pioneered the idea of presenting search results from several categories—web pages, images, videos, books—on the same page, something that Google later adopted. Another popular feature is Naver's "Knowledge Search" service, launched in 2002. It enables people to ask questions, the answers to which are served up from a database provided by other users. If an answer is incomplete or inaccurate, it can be easily changed, Wikipedia-style, for the benefit of others who ask the same question in future. A points system rewards users who submit questions, provide answers or rate the answers provided by other people.

On February 4th NHN announced record sales and profits for 2008, becoming the first South Korean internet company to record sales of more than 1 trillion won ($660m). Such is Naver's grip on the market that Yahoo! and Google have just agreed to combine some of their services in South Korea, in order to give them greater clout against the local giant.

Although Google is having trouble making any headway in South Korea, it may have more of a chance in China, where the market leader, Baidu, has been hit by a series of scandals. Last September, at the height of the scandal over melamine-tainted milk, rumours began to spread that Baidu had accepted payment to expunge stories on the subject from its search results. Baidu denied any wrongdoing. A few weeks later the firm was accused of giving prominence in its search results, in return for payment, to unlicensed drugs companies.

This led to speculation in the local media that web users might be turning against Baidu. Whether or not this is true, it does not help that unlike Google and other rivals, Baidu does not distinguish in search results between paid links (ie, advertisements) and unpaid ones—a practice that was criticised in a report by CCTV, a state-run broadcaster, in November.

As Chinese web users become more sophisticated, they may be gaining a preference for search results that are separate from advertising, which could benefit Google. Advertisers, at least, seem to be switching: the most recent figures suggest that Google increased its market share of internet advertising by 4.4 percentage points during 2008, compared with Baidu's 2.9 percentage points. Baidu has announced plans to delineate more clearly between paid and unpaid links, and has removed links to unlicensed providers of drugs and medical care from its index.

In the Japanese market, meanwhile, Google plays second fiddle to Yahoo! Japan, despite frantic efforts to

catch up by launching more Japan-specific services. It will soon face a new rival, in the form of Naver, which has decided to enter the Japanese market on the basis that Japan, like South Korea, has a unique and distinctive culture and language. After eight years studying and collecting data on Japanese tastes, Mr Chae is confident that Naver can become the leading search engine in Japan—despite the failure of his firm's previous foray into the country, selling search services to companies.

After that, Mr Chae says he plans to launch several more culturally specific search engines, such as "Naver California", "Naver Korean-American" or "Naver Chinese-American". That would be attacking Google on its home turf. Is this too ambitious? Naver say never.

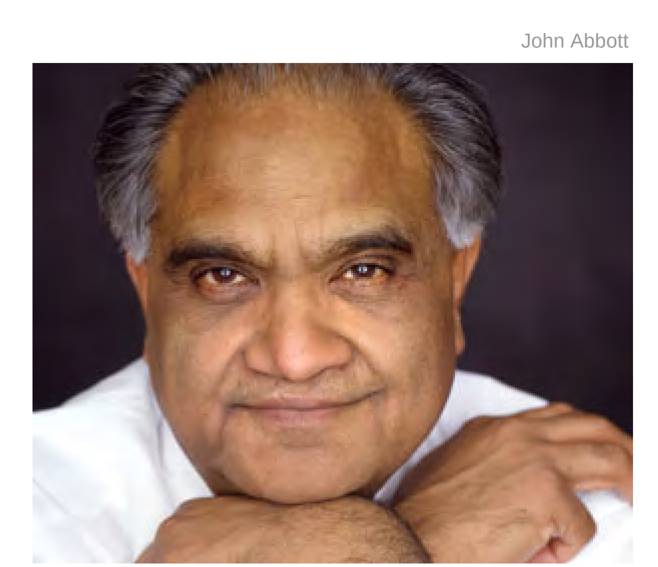
Face value

A teacher for the times

Feb 26th 2009
From The Economist print edition

Ram Charan's no-nonsense business advice resonates in a recession

John Abbott



GROWING up in a small town in the Uttar Pradesh region of India, Ram Charan learnt his most valuable lesson while he was working behind the counter in his family's modest shoe shop. Watching his elders as they advanced credit to customers, who had little money until the next harvest came in, and then juggled the shop's finances to make ends meet, he developed a respect for the importance of carefully managing cashflow. Now a successful consultant, the 69-year-old Mr Charan is using that experience to help his clients in turbulent times.

Although big consulting firms such as Accenture and McKinsey (which this week named Dominic Barton as its new managing director) like to claim that their services are fairly immune to downturns, there are already signs that demand for consultancy is waning. Siemens, a German industrial giant, recently said it would scrap all external advisers to save hundreds of millions of euros. Other firms are likely to follow its lead.

Mr Charan, however, says he is still as busy as ever. That may be because he is something of an oddity in the consulting world. Tom Davenport, a professor at Babson College in Massachusetts who has studied the consulting industry, says it is typically divided between individual gurus who come up with big ideas, publish books, give speeches and undertake the occasional consulting job on the one hand, and the giant consulting firms that take these big ideas and apply them inside corporations using armies of consultants on the other.

The division is not quite so clear-cut in practice. The consultancies, for example, also like to think of themselves as "thought leaders", publishing reams of often-tedious research. Mr Charan bridges both worlds as well, producing plenty of management tomes—his 16th book, "Leadership in the Era of Economic Uncertainty", has just been published—and giving lectures, but also acting as a hands-on consultant to leaders of a host of companies, including Wipro, an Indian outsourcing firm, and DuPont, a chemicals company. It is this immersion in the world of business, through his consulting, that distinguishes Mr Charan from most other popular management thinkers, who often come from academic or journalistic backgrounds. And rather than boasting big-picture themes, his lectures and books often focus on practical suggestions to help managers improve their performance.

Another thing that makes Mr Charan unusual is that few people would want to sign up for the punishing life associated with being both a sage-on-stage and a confidant of many chief executives. A one-man band, Mr Charan is constantly on the move, notching up some 500,000 miles (800,000km) on aircraft

last year and spending most of his nights in hotel rooms. To minimise the amount of baggage he lugs around, assistants at his office in Dallas send fresh clothes to him via courier and his laundry is returned via the same route. Until a couple of years ago, the peripatetic Mr Charan did not even own a home. He has since bought an apartment in Dallas, he says, but he has barely stayed there since he bought it.

He is unlikely to see much of his apartment this year either, however, as his clients clamour for advice on how to deal with the downturn. Mr Charan's main recommendation to managers is to act fast to protect cashflow, even at the expense of, say, boosting earnings per share. Too many executives, he says, still underestimate the likelihood of a prolonged slump and have failed to reduce their companies' "cash break-even points" fast enough. A lack of liquidity has already caused severe headaches for even fundamentally solid companies such as America's GE, which has had to raise fresh capital at punitive rates.

To get through the downturn, Mr Charan says chief executives also need to step up the "intensity" with which they manage. For instance, they should shred annual budgets and instead set targets on a quarterly or monthly basis while the crisis lasts. They also need to develop more "ground-level intelligence"—rapid feedback about what is really happening to their customers and suppliers. No fan of Detroit's leadership over the years, he nevertheless praises Ford for moving quickly to add an extra shift to truck production last November, when the American company spotted that a swift fall in the oil price had led some buyers to consider gas-guzzling vehicles again.

A load of cobblers?

Mr Charan's critics charge that some of his prescriptions border on the simplistic, laced with occasional folksy references to the lessons that he learnt at the shoe shop in India. Yet his clients say that they appreciate his straightforwardness and the fact that, unlike many advisers, he has neither a gargantuan ego nor a pre-cooked framework that he trots out as the solution to every problem. And they appreciate his talent for getting to the nub of a problem quickly. "He's one of the best question-askers I've ever been around," says Tom Lynch, the boss of Tyco Electronics, which counts Mr Charan as one of its board members. Noel Tichy, a professor at the University of Michigan's Ross School of Business who has worked alongside Mr Charan on many projects, describes him as a "wonderful clinician" who can quickly form a diagnosis of what ails a company.

That can include its most senior managers. In his most recent book, Mr Charan warns that there will be many casualties from the recession, including more than a few chief executives. Although he urges boards not to be trigger-happy when bosses miss targets, Mr Charan believes that the skills needed to steer a firm through a deep recession are often different from the ones needed to expand it when the economy is humming. Hence his recommendation that firms brush up their succession plans, if they have not done so already. As his experience in the shoe shop no doubt taught him, there are times when you just have to give somebody the boot.

Economist.com OPINION

American banks

A ghoulish prospect

Feb 26th 2009 | NEW YORK
From The Economist print edition

Nationalisation carries risks, but it may still be the best way to deal with American banking's undead

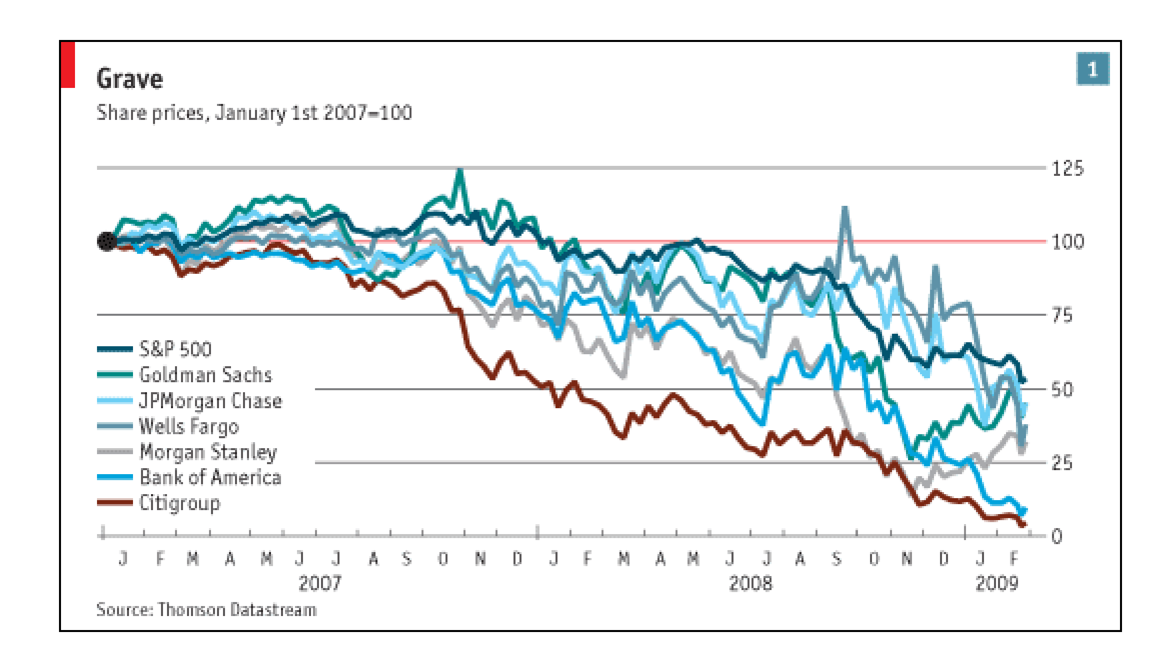
Allstar



IN A classic horror film, "Night of the Living Dead", a terrified group of people barricade themselves in a rural farmhouse to escape hordes of flesh-eating zombies. Today Americans are gripped by a similar fear, but this time the walking corpses in their nightmares are banks, tearing insatiably at the public purse. As the Obama administration struggles to get its poorly received bank-rescue plan up and running, it is being pressed to respond to suspicions that some large banks are on the edge of insolvency, if not already there.

In a matter of weeks nationalisation has gone from taboo to talking point. Economists debate its pros and cons across the blogosphere. Politicians on both left and right accept that America's sickest banks may need to be taken over and restructured and their good parts returned to private ownership. Even Alan Greenspan has become an advocate.

Although the government continues to resist such calls, its hand may be forced by the results of the "stress tests" that it began to perform on February 25th on the 19 largest banks. Officials' own stress levels are running in inverse relation to the banks' share prices. Those of Citigroup and Bank of America plumbed new lows on February 20th (see chart 1). That prompted the Treasury and a group of regulators to declare that they stood "firmly" behind the banking system, but that their "strong presumption" was that banks would remain in private hands. Ben Bernanke, the chairman of the Federal Reserve, went further, saying in congressional testimony this week that nationalisation "is when the government seizes the bank and zeroes out the shareholders…we don't plan anything like that."



Even so, the neediest banks are heading that way. As *The Economist* went to press, the government was in talks with Citigroup over what would in essence be partial nationalisation: the conversion into common equity of a chunk of its preferred stock, obtained in return for pumping capital into Citi last year. This would give it a stake of up to 40%—eight times the holding of Prince Alwaleed bin Talal, the most influential existing shareholder—and voting power to match.

Citi approached regulators about the conversion, fearful of being swamped by further losses as the recession and housing crisis deepen. The deal would mark the bank's surrender in its battle to persuade investors that its reasonably healthy "tier-one" ratio is a convincing measure of capital adequacy. These days markets prefer measures using tangible common equity, which is undiluted by hybrid capital such as preferred stock (see article).

The government may end up repeating this across the industry. The first step in its Capital Assistance Program will be the stress tests, which will take a few weeks. The aim will be to map potential losses in a two-year recession with unemployment rising as high as 10.3% and house prices continuing to tumble. If the testing shows that banks need more capital, they can first try to raise it over six months from private sources. If they fail, they will get government help. The state will take preferred stock (paying a 9% dividend) that converts into common equity if needed.

This strikes some as fiddly at a time when the markets crave boldness. Drip-feeding equity as needed avoids the appearance of nationalisation. But by adding to the complexity of banks' capital structures and not revealing what would constitute adequate capital it risks sowing confusion about their ability to ride out losses.

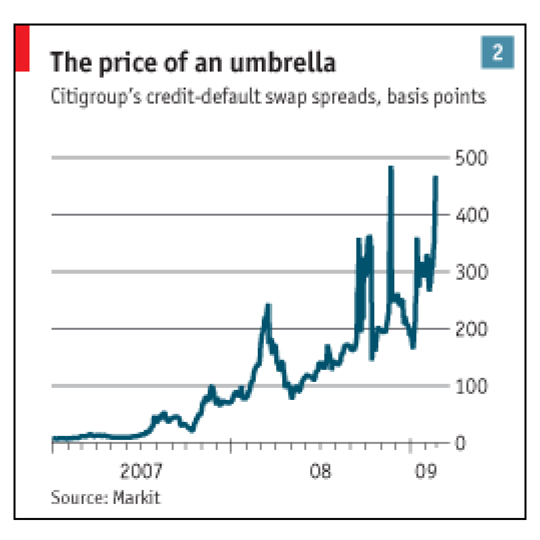
Next for shaving

Nor has the government brought clarity to its treatment of bondholders, which was anything but consistent under the previous administration: Bear Stearns's creditors got their money, Washington Mutual's were all but wiped out. Credit-default swaps on Citi have widened lately (see chart 2), as have those on other big banks. This reflects fears that the state, in return for injecting more capital, might force a "haircut" on creditors, who sit above shareholders in the capital structure.

Compelling troubled banks to default on their debt may seem just. Christopher Whalen, an independent banking analyst, argues that some banks' bondholders may have to take a hit if depositors are to be made whole. The danger, however, is that this causes the sort of liquidity runs that wreaked havoc after the demise of Lehman Brothers last September.

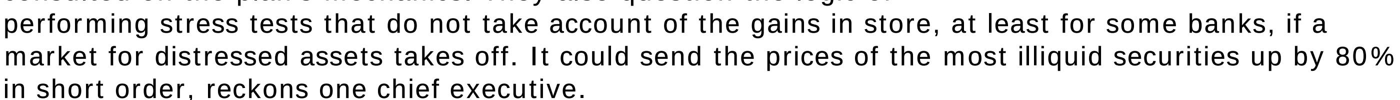
If bond investors are forced to share the pain, they may at least want some potential gain. Some restructuring specialists have suggested that bondholders be handed shares in the most troubled banks through debt-for-equity swaps, a common device

in non-financial corporate workouts. That, however, would leave the banks partly owned by foreign governments and central banks. American politicians may find this unpalatable.



Doubt also surrounds a centrepiece of the bail-out plan announced by Tim Geithner, the treasury secretary, on February 10th: a public-private partnership to buy distressed mortgages and other bad assets. Mr Geithner envisages vulture investors snapping up as much as $1 trillion-worth of the stuff, helped by cheap government loans and perhaps a floor under prices. But details are still being worked on, leaving potential participants sceptical of its merits. Under Hank Paulson, his predecessor, two asset-buying plans foundered after proving unworkable.

Bank executives, meanwhile, are livid that they have not been consulted on the plan's mechanics. They also question the logic of performing stress tests that do not take account of the gains in store, at least for some banks, if a market for distressed assets takes off. It could send the prices of the most illiquid securities up by 80% in short order, reckons one chief executive.



Even if banks can offload at reasonable prices the dross they piled up in the boom, they have lots of other assets that will sour this year, from credit-card debt to corporate loans. High-quality, or "prime", mortgages look ever wobblier, too, as joblessness climbs towards 8%. American banks have recognised more than $1 trillion in credit losses, but most analysts think this is only around half the final tally. The most pessimistic expect losses on American loans to reach $3 trillion-4 trillion.

Regulators insist that the big banks are, by and large, well capitalised despite their flurry of write-offs. Just as important, the industry as a whole is still producing fairly strong cash flows: higher in the rocky third quarter of 2008 than in the calm first quarter of 2007, points out Dick Bove of Rochdale Research.

But this masks huge variation. Some regional banks are thriving, especially those that avoided dodgy mortgages and loans to property developers. Hudson City Bancorp, a New Jersey thrift that wrote only high-quality mortgages through the boom and insisted on down-payments of 20%, recently announced record profits. According to a survey by Greenwich Associates, such conservative lenders are picking up market share from rivals that rely on government support. But Hudson is in the minority. The number of banks on the Federal Deposit Insurance Corporation's problem list was expected to rise sharply, from 171, when the FDIC published its quarterly update on February 26th, after *The Economist* went to press.

Fortunes vary among the giants, too. No one doubts that the sums still needed to put Citi on a sure footing exceed its current market value of about $14 billion. The capital conversion would be its third bail-out in four months. Bank of America is also in poor shape, thanks to its disastrous purchase of Merrill Lynch and its heavy exposure to enfeebled consumers. JPMorgan Chase, the healthiest of the big banks, is nevertheless taking no chances. It cut its dividend this week to save $5 billion in equity. It said this was a precaution, in case conditions worsen dramatically.

What should be done with "systemically important" banks that perform poorly in the stress test? Throwing yet more capital at them risks perpetuating what Paul Krugman, a Nobel prize-winning economist, calls "lemon socialism", in which banks reap the gains but taxpayers eat the losses. It was handouts without proper workouts that led to Japan's "lost decade".

Hence the growing calls for the clean break offered by temporary nationalisation—or "conservatorship", as some prefer. This involves several steps: ascertain which banks are insolvent, take them over, sever the most toxic assets and sell them over time or hold them to maturity. The good parts would be sold to the public or a strategic buyer as quickly as is feasible. These healthy banks would be fit to lend, benefiting the overall economy. The taxpayer may even avoid losses.

This may present another opportunity: to accelerate the break-up of banks that have become too big to fail. This was a problem before the crisis. Shotgun takeovers of weaklings, such as Bear Stearns, Merrill and Wachovia, have made it worse. Citi is considered particularly unmanageable.

Death and taxes

This degree of interference would strike some as un-American. But the government's tentacles are already wrapped around the banking industry, through debt guarantees, loss-sharing agreements, central-bank facilities and capital infusions, not to mention pay caps. It may take up voting rights on its common stock. As Mr Bernanke pointed out this week, banks cannot do whatever they like with capital they receive from the state. Citi already has to clear strategic decisions with regulators.

Moreover, far from being an alien concept, nationalisation is, as Mr Krugman has put it, "as American as apple pie". Banks have often been seized by the state, in the form of the FDIC. Some of them, such as Washington Mutual, have been big. The FDIC runs those with assets that it cannot sell quickly, as it did with IndyMac, a Californian lender, before finding a group of private-equity buyers in January.

Even the most vocal proponents of this approach accept the need to tread with care. Those banks deemed insolvent would have to be dealt with in one go, to avoid the seizure of one bank starting a run on the liabilities of others that are seen as weak, points out Nouriel Roubini of New York University's Stern School.

That is not the only risk. Political owners find it hard not to meddle: they have wasted no time turning America's mortgage agencies and Northern Rock, a British bank, into tools of the state, or arm-twisting banks that took taxpayer money into modifying mortgages. And state control tends to rattle nerves abroad. Mexico's authorities, for instance, are sure to frown on Citi's local subsidiary, Banamex, falling into the hands of another government.

Moreover, the nationalisation of American International Group, an insurer, is no advertisement. In state hands AIG has gone from bad to worse. Already in hock to the taxpayer for $150 billion, it is estimated to have lost another $60 billion in the last quarter of 2008 and is reported to be in talks about a further bail-out and possible break-up. Adding to its woe, the auction of an Asian subsidiary faltered this week.

Then there is the exit strategy. Governments can become attached to banks they get their hands on. Those that resist the temptation cannot always find buyers. It took the FDIC seven years to sell Continental Illinois, which failed in 1984. Sweden deftly managed its overhaul and flotation of bust banks in the 1990s, but its financial system was much smaller and simpler than America's today.

Finally, government takeovers are risky amid a systemic crisis because of the scale and distribution of creditors' potential losses. Jeffrey Gordon of Columbia Law School cites Citi as an example. With total liabilities of $1.9 trillion and deposits of just $800 billion, not all of them insured, it has over $1.1 trillion of claims at risk in the event of a seizure. Their value would depend on how much the receiver would get for the bank's assets. Were it to push for a quick sale, the price would doubtless be low, clobbering creditors that included pension and money-market funds. Though full-blown nationalisation "appeals to the desire for a clean sweep and the punitive distribution of losses", it is, Mr Gordon argues, a gamble.

Is there a way to deal with bombed-out banks that falls short of greatly increased government ownership? Some, nostalgic for the past, point to the Latin American debt crisis of the 1980s. Then, Western regulators went soft on their banks, allowing even the insolvent to limp along until they had regained enough strength to withstand the Brady-bond restructuring. But that is an imperfect parallel. The economy was in better shape, so it was easier for banks to return to health. And there was no mark-to-market accounting. Suspending that today would ease the burden on banks, but would also make it easier to avoid admitting to losses.

With such forbearance unlikely this time, greater state control seems inevitable, despite its drawbacks. To keep recapitalising hopelessly insolvent banks without more draconian measures merely necessitates further bail-outs, argues Joseph Mason, an expert on banking crises at Louisiana State University. He suggests the Depression as a model: the Reconstruction Finance Corporation ended up with effective control over large parts of the banking system. It used its power to fire executives and shake up operations, with dramatic results. In each successive crisis, he says, authorities have to relearn the lessons applied by private-equity firms: "Keep control of the firm and the capital."

That is hard to swallow in a country that likes its capitalism red in tooth and claw. But better a temporary ward of the state than a permanent zombie.

Bank capital

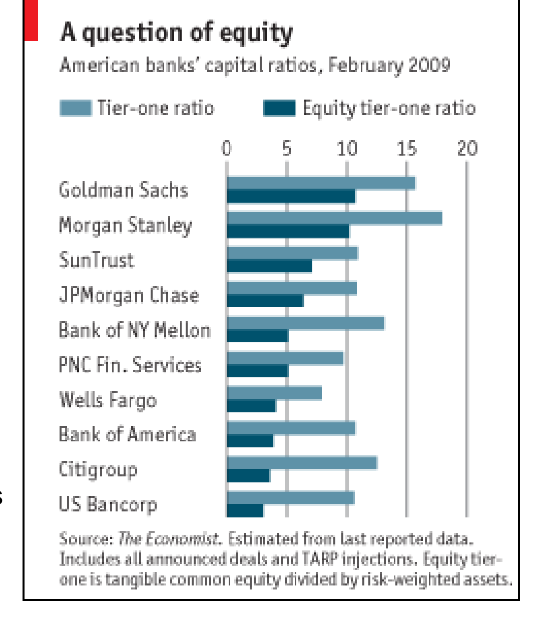
Stress-test mess

Feb 26th 2009
From The Economist print edition

American regulators are "stress testing" banks. What might be the result?

ASSESSING banks' capital adequacy has become almost as tortured as trying to work out their exposures to toxic credit. Disclosure is patchy and a plethora of measures exists, with most banks emphasising those that flatter them most. American regulators hope to clean up the mess by imposing stress tests on lenders and requiring them to raise new capital, probably from the government, to plug any shortfalls. Behind the scenes such a test will probably require banks to meet a given, but undisclosed, standard of capital adequacy. It will also involve checking that asset valuations reflect the possibility of a severe recession.

Judged by tier-one capital, a common measure of adequacy, America's ten biggest banks by assets appear in reasonable shape. Typically, their ratios of tier-one capital to risk-weighted assets exceed 10% (see chart). However, the quality of their tier-one capital has crumbled. Only about half now consists of tangible common equity, the purest and most flexible form of capital which bears the "first loss" when an asset goes sour. The rest is largely preference stock, much of it government-owned, which is not truly loss-bearing. For example, the dividends on Citigroup's government preference shares can be deferred but not cancelled, unlike those on common stock. The original Basel rules on capital adequacy sought to limit such "hybrid" capital that sits between equity and debt. But most governments like preference stock because it does not carry votes, and thus avoids nationalisation, and because the more secure dividends protect taxpayers, providing the bank does not go bust.



Source: *The Economist*. Estimated from last reported data. Includes all announced deals and TARP injections. Equity tier-one is tangible common equity divided by risk-weighted assets.

Markets, however, have not been playing ball. In the past two weeks the share prices and, more scarily, the credit spreads of banks with the lowest-quality tier-one capital have deteriorated sharply. This suggests the new stress test should target "equity tier-one" capital, which strips out preference stock. The simplest way to bolster this is to convert state preference shares into common equity. This has already happened in Britain, at Royal Bank of Scotland, and has been discussed at Citi.

In theory, how much common equity might America's top ten need? Suppose they had to hit JPMorgan's equity tier-one ratio of 6.4%. Although the bank has just cut its dividend it still views its balance sheet as a "fortress", and the safest European banks have similar ratios. Six banks would fail this test. They would need an estimated $107 billion of new common equity in total. The state has already invested about $130 billion of preference stock in these firms. So by switching this into common shares regulators could get the laggards up to the mark. If this were done at market prices, Bank of America and Citi would pass into majority government control. The state would have big minority stakes in PNC Financial Services, US Bancorp and Wells Fargo.

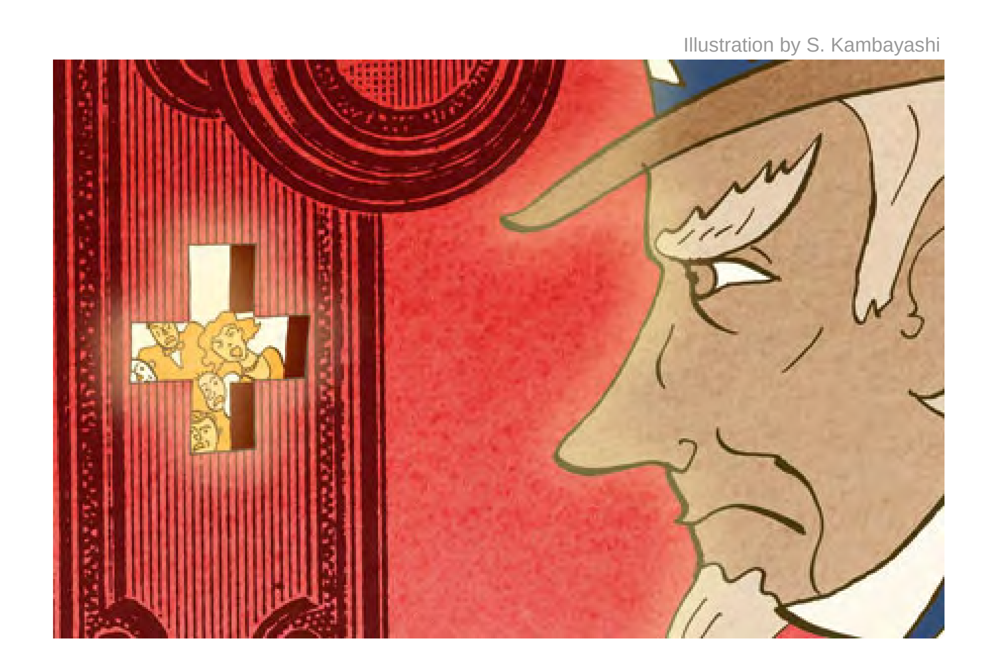
Unfortunately, anxious to avoid such overt intervention, the government has opted for half-measures. Its desired equity tier-one ratio remains unknown. Any hole will be filled by exotic preference stock that will turn into common equity only as losses materialise. If this fuzziness is not enough to spook investors, the other component of the test, the checking of asset values, may well be. Although the government seems keen to talk up banks' balance sheets, lenders' records and the deterioration of the economy mean that further big write-downs cannot be ruled out.

UBS

Called to account

Feb 26th 2009
From The Economist print edition

Illustration by S. Kambayashi



UBS pays the price of its American follies with a galling change of leadership

PRIVATE banking is meant to be boring. But somehow UBS, the world's largest private bank, forgot that. Some of its employees, in their zeal to win the business of wealthy Americans with a predilection for fibbing to the taxman, seem to have confused discretion with spycraft. Instead of waiting for clients to come to it in Switzerland, the bank trained some members of staff in counter-surveillance techniques, equipped them with encrypted laptops and secret e-mail addresses and then infiltrated them into America to meet clients, according to American prosecutors.

The price of such subterfuge has been high. On February 18th UBS agreed to pay fines of $780m and to hand the American authorities the names and account details of up to 300 clients. A week later Marcel Rohner, its youthful chief executive, unexpectedly stepped down.

Although he is credited with having salvaged what he could of UBS by raising capital early, and he helped it withstand steep losses and a slumping share price during 20 months at the helm, Mr Rohner could not, it seems, entirely escape his past. Although not accused of any wrongdoing, he was head of the wealth-management business when many of the shenanigans are alleged to have occurred.

More galling, perhaps, is that Mr Rohner was replaced by Oswald Grübel, a veteran former chief executive of Credit Suisse, UBS's archrival. Mr Grübel unashamedly copied UBS's strategy of combining commercial, investment and private banking, but without the missteps that led UBS so disastrously into American subprime mortgages. UBS shares rose immediately after his appointment, but he has a huge task ahead of him. Not least is the damage UBS's private bankers have done over the bank's, and its home country's, reputation for bank secrecy.

Their antics paid handsomely for a while. The offshore-banking business of UBS gathered some $20 billion in assets from at least 20,000 American clients, earning the bank some $200m a year, according to prosecutors. The government reckons that some 17,000 of these clients omitted to mention their numbered Swiss bank accounts when filling in their American tax returns. Although illegal in America and most other parts of the world, under Swiss law this is no crime.

There may be a fine distinction between someone who has simply forgotten to include everything on a tax return (an oversight that even treasury secretaries are occasionally prone to) and someone who has gone

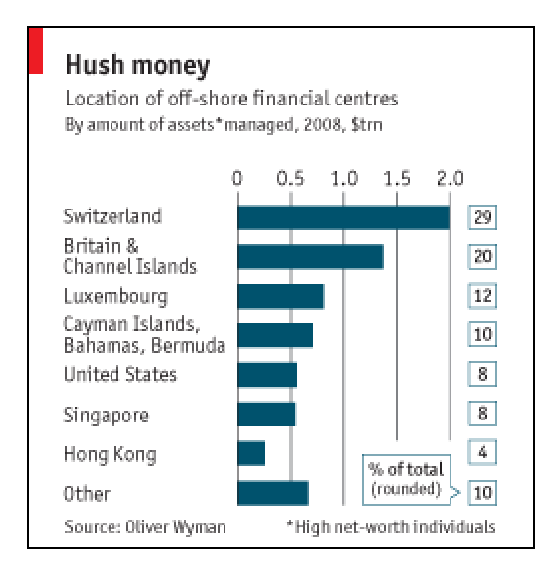
out of their way to evade tax. Yet fraud is illegal in Switzerland as well as in America.

UBS seems to have crossed the line, either by helping some clients set up dummy companies and sham accounts to hide money from the taxman, or by turning a blind eye when they did. The number of clients who did this was small, about 250, but by helping them UBS not only exposed itself to prosecution in America but also endangered Switzerland's status as a secretive piggy-bank for the world's rich.

It was a capitulation shared with Switzerland's financial regulator, which allowed UBS to release their names, saying that a criminal prosecution could ultimately have put the bank's existence at risk. But it was not a total cave-in. The bank and Swiss authorities are still hewing to the distinction in Swiss law between sins of omission and of commission. They will, for instance, contest in court a separate demand from America's Internal Revenue Service (IRS) that UBS hand over the names of the 52,000 American account-holders it is thought to have.

Even a partial surrender, however, may spook wealthy clients. Champions of bank secrecy see it as the fraying of a tradition that has withstood wars, pressure from powerful states and the prying eyes of foreign spies. "They are trying to save UBS because it is systemically important but they are sacrificing the rest of us," says Konrad Hummler, who heads the Swiss Private Bankers Association.

At risk is up to $2 trillion in offshore assets held in Swiss private banks (see chart). There are also important questions at stake about the reach of the state and a citizen's right to privacy.



Those who press for an end to banking secrecy argue that people who hide their assets have shifty motives, such as to avoid paying taxes. That includes John DiCicco, of America's Justice Department, who pointed to the millions of Americans losing their jobs, homes and health care while "more than 50,000 of the wealthiest among us have actively sought to evade their civic and legal duty to pay taxes". Some say as much as $255 billion a year slips through tax nets around the world.

Yet many rich people want to keep their money away from prying eyes for reasons other than to avoid tax, including those fearing divorce settlements. Others want to keep their money safe from expropriation by fickle governments, and hidden from thieving criminals.

Stefan Jaecklin, of Oliver Wyman, a consultancy, reckons that much of the new money that flowed into Switzerland in recent years came from countries with low or no personal income taxes, such as the Gulf, and that a rapidly increasing share of money coming from European countries with high rates of tax is declared to the authorities. The lure, he says, is not only the secrecy but also the industry's well-established competence.

Even the most ardent defenders of banking secrecy concede that the tide is turning against it, however. In the rich world, the mood against all big banks has soured, including offshore ones. At the G20 meeting in April, European leaders want to discuss potential sanctions against tax havens that refuse to hand over information held by their banks.

Mr Grübel, as much as anyone in Switzerland, has a huge stake in the outcome of this debate. For all the problems he faces managing the investment bank, the private bank is still crucial to UBS's survival.

Dubai's bail-out

The outstretched palm

Feb 26th 2009
From The Economist print edition

Abu Dhabi bails out its neighbour. What will it ask in return?

THE Jebel Ali port in Dubai boasts of being the largest man-made harbour in the world. Its “quad-lift” cranes can hoist four 20-foot containers at once. The port’s second terminal will raise its capacity to 14m containers. But plans for a third terminal look premature. Dubai is suffering from a slump in the trading, lending, holidaying and profiteering that buoyed this remarkable emirate for so long.

On February 22nd Dubai was hoisted out of its financial trouble by its oil-rich neighbour, Abu Dhabi. The central bank for the United Arab Emirates (UAE) bought $10 billion-worth of Dubai’s five-year bonds. The bail-out confirmed everyone’s assumption that Abu Dhabi would not let the second-biggest member of the UAE fail. But its benefactor waited long enough to plant a seed of doubt in people’s minds. In recent weeks, the spreads on credit-default swaps for securities issued by Dubai’s government and several of its biggest corporations have widened alarmingly, if a little hysterically.

Having long ago depleted most of its oil reserves, Dubai has reinvented itself as a “sell-side” emirate, dreaming up ingenious schemes for other people to invest in. Chris Davidson of Durham University, who has written a history of the emirate, describes it as a “spongelike economy”, designed to absorb foreign money. The government imposes few levies (Dubai has no income tax) and accounts for only $10 billion of the emirate’s debts. But its rulers sponsor an extended family of companies. Between them, these corporations have amassed about $70 billion of liabilities (see chart), adding to a debt pile that almost matches the emirate’s 2008 GDP of $82 billion.

He ain’t heavy
Dubai’s debts, 2007-08, $bn

Central Government	10.0
Nakheel	7.3
DP World	5.8
Borse Dubai	3.8
Emirates Group	3.7
Emaar Properties	2.4
Other companies	47.0
Total	**80.0**

Source: Moody’s

On the other side of Dubai’s ledger, the government claims to have $90 billion in assets on top of the $260 billion held by its corporations. But it has not revealed the composition or liquidity of its holdings. The very fact that it had to turn to its neighbour for help suggests that its own family silver is not that easy to sell.

The bond proceeds will allow Dubai to meet its obligations this year (which amount to about $10 billion-15 billion) and probably next. But what will Abu Dhabi ask in return? On the face of it, not much. Tristan Cooper, of Moody’s, a rating agency, had expected Abu Dhabi to be “a bit more fussy” about how the funds were used. It might, say, have taken equity stakes in Dubai’s freewheeling corporations or sought some control over their managers.

But Mr Davidson thinks the unstated price of Abu Dhabi’s support will be stiff indeed. “It is the end of the second emirate’s economic autonomy, which it has fiercely protected,” he says. Why else did Abu Dhabi put Dubai through “months of pain and humiliation”, if it did not see some long-term gain from chastening its neighbour and strengthening the UAE federation, Mr Davidson asks. Dubai will now have to be more accommodating of its neighbour’s wishes, he says. It will, for example, have to forgo its independent foreign policy, which had seen it become Iran’s outlet to the world, even as Abu Dhabi kept a careful distance.

Dubai will also have to “lose its ambitions to become the Monaco of the Gulf,” Mr Davidson says. Abu Dhabi will insist on greater prudence and Dubai’s go-getting rulers may also now feel defeated. Their economic ambitions were driven partly by their political insecurities. “A lot of the urgency we saw in the last ten years was fuelled exactly by Dubai’s need to keep its autonomy,” Mr Davidson says.

But for all Dubai’s woes, the Gulf still needs a financial centre, a port, and a secure place to live, Mr Cooper points out. With a little less gumption and a lot less gearing, “Dubai is plausible”.

Gold

Haring away

Feb 26th 2009
From The Economist print edition

Burnished by bad news, gold looks like a good each-way bet

IT IS 1979 and Harry “Rabbit” Angstrom, the hero of John Updike’s series of novels, is explaining to his wife why he has just spent more than $11,000 on 30 gold krugerrands. “The beauty of gold is, it loves bad news,” he says. Three decades later, gold is once again thriving on despair. Before Christmas, a troy ounce could be bought for around $800. By the third week in February, gold was trading at close to $1,000 an ounce.

A surge in demand for gold as an investment lies behind the jump in prices. Flows into exchange-traded funds, which buy and store gold for their shareholders, rose from 105 tonnes in January to 208 tonnes in the first three weeks of February, according to Suki Cooper at Barclays Capital. At that rate, inflows will soon surpass the total of 322 tonnes for the whole of 2008. Buying by investors has more than made up for a slump in gold-jewellery purchases in key markets, such as India and Turkey, where higher prices and wilting exchange rates have crushed demand.

People have long viewed gold, rightly or wrongly, as a hedge against high inflation and a weak dollar. So when the gold price briefly broke through the $1,000 mark in March last year, it was easily explained by fears that rising commodity prices (and, in America, a weak dollar) would feed inflation. An earlier run-up in gold prices, between 2002 and 2005, coincided with a sustained fall in the dollar. But now gold is strong even as the dollar thrives and economies face deflation.

Gold’s recent progress seems to be a response to generalised fears of economic turmoil. When supposedly safe savings vehicles, such as bank deposits, look shaky and offer scant returns, gold has greater appeal as an alternative store of wealth. It also looks like an attractive each-way bet. If drastic cuts in interest rates work too well, that will fuel inflation. If they do not work, prices of assets, such as stocks and houses, will sink further.

Like Updike’s protagonist in “Rabbit is Rich”, the new wave of gold investors typically have wealth to preserve, according to Adrian Ash at BullionVault, an online service for gold investors. “Gold is something you buy if you have something to lose,” he says. What links today’s gold fever with the 1970s rush is negative real deposit rates. Many savers now prefer a claim on gold in a vault to one on cash in the bank. There is less risk that a counterparty blows up, and the “carrying cost” of gold in terms of lost interest is, in any case, vanishing.



How high might the gold price go? Gold bugs talk excitedly about it reaching $2,300, which would match the January 1980 peak in real terms (see chart). Already the gold price is above its average since 1972 when calculated in today’s money. There is a limited supply of gold and lots of potential buyers—ideal conditions for a bubble, says Stephen Jen at Morgan Stanley. If gold is burnished by grim news, it seems likely to become still more alluring.

Ayn Rand

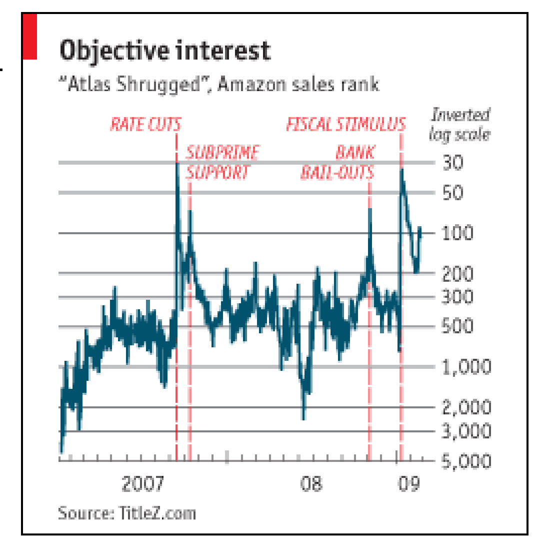
Atlas felt a sense of déjà vu

Feb 26th 2009
From The Economist print edition

The economic bust has caused a boom for at least one author

BOOKS do not sell themselves: that is what films are for. “The Reader”, the book that inspired the Oscar-winning film, has shot up the bestseller lists. Another recent publishing success, however, has had more help from Washington, DC, than Hollywood. That book is Ayn Rand’s “Atlas Shrugged”.

Reviled in some circles and mocked in others, Rand’s 1957 novel of embattled capitalism is a favourite of libertarians and college students. Lately, though, its appeal has been growing. According to data from TitleZ, a firm that tracks bestseller rankings on Amazon, an online retailer, the book’s 30-day average Amazon rank was 127 on February 21st, well above its average over the past two years of 542. On January 13th the book’s ranking was 33, briefly besting President Barack Obama’s popular tome, “The Audacity of Hope”.



Tellingly, the spikes in the novel’s sales coincide with the news (see chart). The first jump, in September 2007, followed dramatic interest-rate cuts by central banks, and the Bank of England’s bail-out of Northern Rock, a troubled mortgage lender. The October 2007 rise happened two days after the Bush Administration announced an initiative to coax banks to assist subprime borrowers. A year later, sales of the book rose after America’s Treasury said that it would use a big chunk of the $700 billion Troubled Asset Relief Programme to buy stakes in nine large banks. Debate over Mr Obama’s stimulus plan in January gave the book another lift. And sales leapt once again when the stimulus plan passed and Mr Obama announced a new mortgage-modification plan.

Whenever governments intervene in the market, in short, readers rush to buy Rand’s book. Why? The reason is explained by the name of a recently formed group on Facebook, the world’s biggest social-networking site: “Read the news today? It’s like ‘Atlas Shrugged’ is happening in real life”. The group, and an expanding chorus of fretful bloggers, reckon that life is imitating art.

Some were reminded of Rand’s gifted physicist, Robert Stadler, cravenly disavowing his faith in reason for political favour, when Alan Greenspan, an acolyte of Rand’s, testified before a congressional committee last October that he had found a “flaw in the model” of securitisation. And with pirates hijacking cargo ships, politicians castigating corporate chieftains, riots in Europe and slowing international trade—all of which are depicted in the book—this melancholy meme has plenty of fodder.

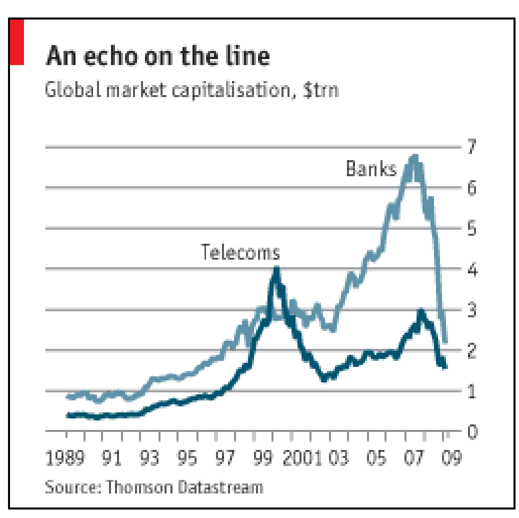
Even if Washington does not keep the book’s sales booming, Hollywood might. A film version is rumoured to be in the works for release in 2011. But by then, a film may feel superfluous to Rand’s most loyal fans; events unfolding around them will have been dramatisation enough.

Lessons from the telecoms bubble (1)

Crash course

Feb 26th 2009
From The Economist print edition

What can banks learn from the clean-up after the telecoms crash of 1997-2003?



BEFORE banks, the last global industry to commit collective suicide was telecoms during the boom and bust of 1997-2003. The parallel is imperfect—banks are uniquely vulnerable to runs and have a special role in the economy. Reflecting this, only a few telecoms companies received state bail-outs. But in a narrower corporate sense, the meltdown rivalled that of the banks. From peak to trough the industry lost $2.8 trillion of market value, compared with the $4.6 trillion banks have shed (see chart). Just like banks, telecoms had imperial bosses, kamikaze deals and incomprehensible jargon—if collateralised-debt obligations troubled you, try gigabit Ethernet routers. In telecoms leading firms were reduced to indebted objects of ridicule. The consequences were bankruptcies, huge job losses, fraud, trashed reputations and, eventually, a clean-up.

By these standards, banks remain in a fantasy world. They are largely still run by the same people, they have a piecemeal approach to cutting leverage, and their goal, beyond firefighting, is to tinker with their portfolios, removing areas of egregious excess. If the telecoms industry is anything to go by, this gradualism will fail. A management cull is both inevitable and desirable—only a handful of telecoms bosses clung on and prospered, Ivan Seidenberg of Verizon being one example. Firms, like Vodafone, that took an evolutionary approach to replacing the old guard regretted it, with rows souring the boardroom for years. Complacency can kill even the biggest firms. The two leading telecoms firms of the 1990s, AT&T (since bought by SBC, which took its name) and British Telecom, were more or less dismantled by investors tired of their flawed cultures and incoherent empires. Bank conglomerates like Citigroup should take note.

What should new managers do first? Define a core business and be brave enough to raise the equity to fund it. Those telecoms firms, such as Telecom Italia, that failed to cut their debt went on to shrink into obscurity. Too many others chose expedient fire sales, especially of emerging-market assets. Banks look vulnerable to this, since governments want them to bolster their domestic balance-sheets, but the telecoms firms that did best were those, like Spain's Telefónica, that clung to the assets that promised growth.

Telecoms companies, like banks today, were encouraged to go “back to basics”. But once they wiped away the froth, their core businesses were mature and mediocre—as banks will discover with their branches. That raised the temptation for acquisitions. Sadly for the telecoms firms, bottom-fishing for distressed assets rarely worked, and investors vetoed empire-building deals involving mature assets that yielded few cost synergies. Even domestic deals had mixed results. In America SBC successfully swallowed several rivals, but the merger of Sprint and Nextel, two mobile-phone firms, was ruined by bad execution. This pattern of European ossification and American consolidation is holding true for banks. Doubtless the difficulties of meshing combinations like Bank of America/Merrill Lynch and Wells Fargo/Wachovia during a downturn are being underestimated.

Next, new bosses must start a cultural revolution. Bubbles corrupt firms' intellectual capital; in telecoms, everything from sales incentives to budgeting had become based on measures that had little to do with a sober view of profits. The rot reached the top, with investors, directors and managers evaluating performance using cashflow models that were so long-dated that they broke even after their authors planned to retire. This problem is deeply embedded in banks, where most common measures—return on equity, cost/income ratios and price/earnings ratios—flatter leveraged firms, and where a culture of giving cheap capital to high-risk units has thrived. Bank bosses must create a new financial language and may find they are treated as heretics when they do so.

Ideally, this revolution can be extended to reinventing brands and business models. But a depressing precedent has been set by incumbent telecoms firms, which, like most banks, are stodgy bureaucracies at heart. Despite endless product launches and reorganisations, perhaps only two firms, KPN (see article) and O2 (subsequently bought by Telefónica) were transformed by innovative managers. For most others, the decade since the bubble has been a slog against competitors and reinvigorated regulators. That is the lot of most firms in most industries. They face a constant battle to protect pockets of high profits and have few chances to grow. For telecoms, the glamour and infamy were followed by mediocrity. Banks are still staggering about in the limelight, but the same fate surely awaits them.

Lessons from the telecoms bubble (2)

Adulation

Feb 26th 2009
From The Economist print edition

Tips on taking charge of a basket case in a broken industry, from KPN's boss

AD SCHEEPBOUWER is the nearest thing the telecoms industry has to an action hero. For anyone parachuted in to turn round troubled banks, he has a move or two worth learning.

When he arrived as chief executive at KPN in 2001, the Dutch operator had been wrecked by the bubble. Net debt was six times operating profits and some employees were "living in an illusion", he says. "I told them: 'You could do business with me or the receiver'."

First, he persuaded banks to give KPN some breathing space and convinced shareholders to back a rights issue. He also hired a team of external consultants to search the firm's books for unexploded ordnance. There were also "dozens of hobby projects" that had to be shut down, with even minor capital-spending decisions subject to board review. And there were big job cuts.

On disposals, KPN trod a fine line skilfully. Minority stakes were "dead money" and sold, whereas alliances with other firms were unwound to remove complexity. But KPN also bought assets where necessary, even in the midst of the crisis, taking full control of its growing but troubled German mobile unit—a very significant move.

By 2004 KPN was off life-support, but Mr Scheepbouwer wondered "what the hell we were going to do next". The answer was the then-radical policy of selling multiple mobile brands on one network, which transformed KPN's prospects in Belgium and then Germany. Mr Scheepbouwer plans to stay until at least next year, when he expects dividends per share to be about 50% above the level in the peak bubble year of 1999. If banks can match that by 2019, they will be doing well.

Economist.com



Economics focus

Domino theory

Feb 26th 2009
From The Economist print edition

Where could emerging-market contagion spread next?

THE drought of foreign capital is beginning to wreck many economies in central and eastern Europe. Currencies, shares and bonds are tumbling, and some economists fear that one or more of these countries could default on its foreign debts. Emerging-market crises have a nasty habit of spreading as investors flee one country after another. Some Middle Eastern markets, notably Dubai, are already in trouble. But which of the larger emerging economies are most vulnerable?

To answer that question in the past, economists used to pay most attention to the solvency of governments, and hence their debt-to-GDP ratios. But today, the biggest risk in the emerging world comes not from sovereign borrowing, but from the debts of firms and banks. As foreign capital dries up, they will find it harder to refinance maturing debts or to raise new loans.

If one green bottle should accidentally fall...

Country	Current-account as % of GDP*	Short-term debt as % of reserves*	Banks' loan/ deposit ratio	Overall risk ranking†
South Africa	-10.4	81	1.09	17
Hungary	-4.3	79	1.30	16
Poland	-8.0	38	1.03	14=
South Korea	1.3	102	1.30	14=
Mexico	-2.5	39	0.93	12=
Pakistan	-7.8	27	0.99	12=
Brazil	-1.5	22	1.36	10=
Turkey	-2.3	70	0.83	10=
Russia	1.5	28	1.51	9
Argentina	0.2	63	0.74	8
Venezuela	0.8	58	0.75	7
Indonesia	1.2	88	0.62	6
Thailand	0.3	17	0.88	5
India	-2.4	9	0.74	4
Taiwan	7.9	26	0.87	3
Malaysia	11.3	15	0.72	2
China	5.2	7	0.68	1

Sources: HSBC; Economist Intelligence Unit *2009 forecast †Higher score implies higher risk

Our table (based largely on figures provided by HSBC) uses three indicators to judge how vulnerable economies are to the global credit crunch. The first is the expected current-account balance for this year. Large deficits need to be financed, but banking and portfolio inflows are now scarce, and even foreign direct investment, which used to be seen as less volatile, has fallen sharply this year. Many of the smaller east European economies had double-digit deficits as a share of GDP in 2008, although deep recessions will reduce them this year. Among the countries in the table, Pakistan, South Africa and Poland are tipped to run current-account deficits of 8% or more of GDP this year—the size of Thailand's deficit before its crisis in 1997.

As well as financing a current-account shortfall, a country has to repay or roll over existing debts. If external finance is not available, it must run down its reserves. Thus a useful measure of financing risk is short-term debt (due within 12 months) as a percentage of foreign-exchange reserves. Anything above 100%, implying that debts exceed foreign exchange, should ring alarm bells. (At the start of 1997 Thailand's short-term debt was 130% of its reserves.) The ratio is estimated at over 250% in both Latvia and Estonia, but in all the larger emerging economies it is below 100%. However, HSBC forecasts that South Korea's short-term debt will exceed its shrinking reserves before the year is out. The reserve cover

in Indonesia, South Africa and Hungary is also looking thin. Russia's reserves have plunged by more than one-third as the central bank has tried to prop up the rouble, but it still has a comfortable cushion.

The third indicator, the ratio of banks' loans to their deposits, is one measure of the vulnerability of banking systems. When the ratio is over 1.0 (as in, say, Russia, Brazil, South Korea and Hungary), it means that the banks depend on borrowing, often from abroad, to finance domestic lending and so will be squeezed by the global credit crunch.

To get an overall sense of financial vulnerability we have ranked all the countries on each of the three measures and then taken their average score. If all emerging economies were included, the smaller east Europeans, such as Latvia, Ukraine and Romania, would dominate the top of the risk league. Among the 17 larger economies shown in the table, South Africa and Hungary look the most risky; China the least. Hungary has already had to go cap in hand to the IMF for a loan. South Africa may yet have to. Despite higher gold prices, weaker mineral exports are causing its current-account deficit to swell, possibly to more than 10% of GDP this year, at the same time as net foreign direct investment is expected to slump, so the country needs to borrow even more. The rand, which has already fallen sharply, remains one of the most vulnerable emerging-market currencies.

Not again

In contrast, the Asian emerging markets generally look the safest, taking all six slots at the bottom of the table. The main exception is South Korea, which, thanks to its large short-term foreign debts and highly leveraged banks, is deemed to be as risky as Poland. (Vietnam, though not included in the table, also scores high on the risk rating). South Korea is in much healthier shape than during the 1997-98 crisis. For example, it is expected to move back to a small current-account surplus this year and its reserves are much larger. But its banks and its currency still look vulnerable. The won has already fallen by almost 40% against the dollar over the past year, swelling the local-currency value of its foreign debts. Increased financial jitters in east Europe could make it harder for South Korea to roll over the $194 billion debt which falls due this year. But currency-swap agreements with America, Japan and China will give it plenty of firepower to draw on.

The overall score in the table only ranks countries' relative risks. To assess the absolute risk of a crisis you need to estimate external-financing needs (defined as the sum of the current-account balance and the stock of short-term debt) over the next 12 months. Jonathan Anderson, at UBS, has calculated the gap between this and the stock of foreign-exchange reserves for 45 countries. The good news is that only 16 of them have a financing “gap”; in all the others, reserves are more than sufficient to cover a year's worth of payments, even if there were no new capital inflows. Virtually all of those 16 countries are in central and eastern Europe. They include only two large emerging economies from outside the region: Pakistan, which already has an IMF programme, and South Africa. By contrast, South Korea should not have a financing gap, thanks to its expected move back into current-account surplus. Most emerging economies' large reserves will help to keep them out of danger. Unfortunately, the longer that the credit crunch continues, the more those reserves will start to dwindle.

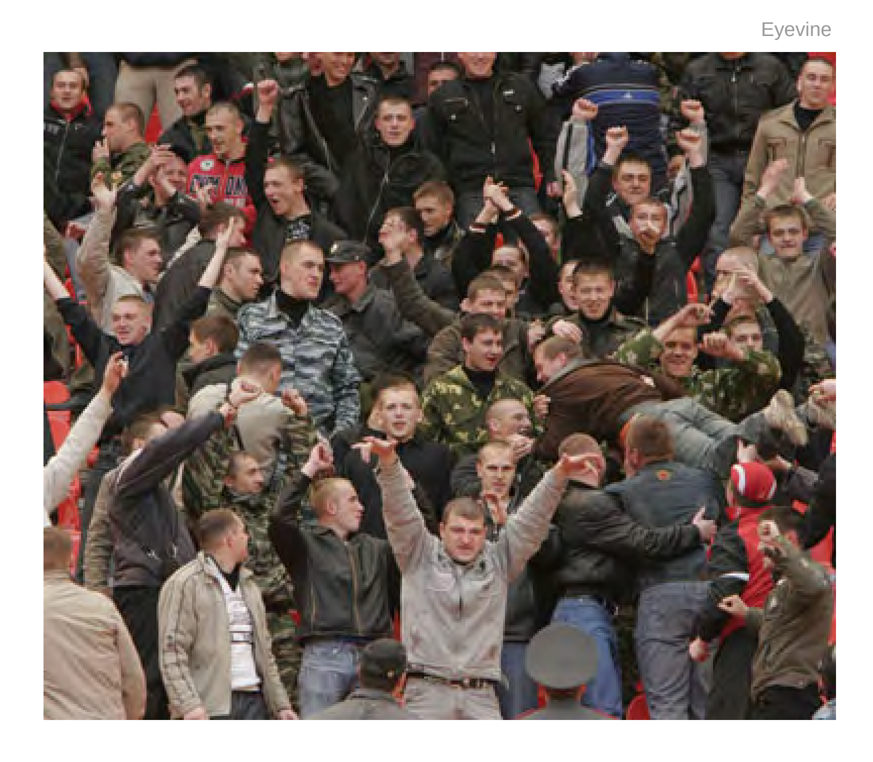
Public order

The kindness of crowds

Feb 26th 2009 | LAUSANNE
From The Economist print edition

Crowds of people are often seen as bad for public order. But they have ways of policing themselves that the police might do well to understand

Eyevine



ACCORDING to a much-reported survey carried out in 2002, Britain then had 4.3m closed-circuit television (CCTV) cameras—one for every 14 people in the country. That figure has since been questioned, but few doubt that Britons are closely scrutinised when they walk the streets. This scrutiny is supposed to deter and detect crime. Even the government's statistics, though, suggest that the cameras have done little to reduce the worst sort of criminal activity, violence.

That may, however, be about to change, and in an unexpected way. It is not that the cameras and their operators will become any more effective. Rather, they have accidentally gathered a huge body of data on how people behave, and particularly on how they behave in situations where violence is in the air. This means that hypotheses about violent behaviour which could not be tested experimentally for practical or ethical reasons, can now be examined in a scientific way. And it is that which may help violence to be controlled.

One researcher who is interested in this approach is Mark Levine, a social psychologist at Lancaster University in Britain who studies crowds. Crowds have a bad press. They have been blamed for antisocial behaviour through mechanisms that include peer pressure, mass hysteria and the diffusion of responsibility—the idea that "someone else will do something, so I don't have to". But Dr Levine thinks that crowds can also diffuse potentially violent situations and that crime would be much higher if it were not for crowds. As he told a symposium called "Understanding Violence", which was organised by the Ecole Polytechnique Fédérale de Lausanne in Switzerland earlier this month, he has been using CCTV data to examine the bystander effect, an alleged phenomenon whereby people who would help a stranger in distress if they were alone, fail to do so in the presence of others. His conclusion is that it ain't so. In fact, he thinks, having a crowd around often makes things better.

Crowd control

The dynamics of crowd behaviour are hard to study, not least because people are not reliable witnesses of their own behaviour. But Dr Levine persuaded the authorities in one British city to allow him to look at their CCTV footage of alcohol-fuelled conflict in public places, suitably anonymised to comply with privacy and data-protection laws. He analysed 42 clips of incidents that operators in a control room had judged had the potential to turn violent, though only 30 of them actually did so. He recorded gestures he labelled either “escalating”, such as pointing and prodding, or “de-escalating”, such as conciliatory open-handedness.

His first observation was that bystanders frequently intervene in incipient fights. The number of escalating gestures did not rise significantly as the size of the group increased, contrary to what the bystander effect would predict. Instead, it was the number of de-escalating gestures that grew. A bigger crowd, in other words, was more likely to suppress a fight.

Some incidents did end in violence, of course. To try to work out why, Dr Levine and his colleagues constructed probability trees to help them calculate the likelihood that a violent incident such as a punch being thrown would occur with each successive intervention by a bystander. Using these trees, they were generally able to identify a flashpoint at which the crowd determined which way the fight would go.

Judging the fight to begin with the aggressor’s first pointing gesture towards his target, the researchers found that the first intervention usually involved a bystander trying to calm the protagonist down. Next, another would advise the target not to respond. If a third intervention reinforced crowd solidarity, sending the same peaceful message, then a violent outcome became unlikely. But if it did not—if the third bystander vocally took sides, say—then violence was much more likely.

Dr Levine talks of a “collective choreography” of violence, in which the crowd determines the outcome as much as the protagonist and the target do, and he is now taking his ideas into the laboratory. In collaboration with Mel Slater, a computer scientist at University College, London, he is looking at the responses of bystanders to violence recreated in virtual reality.

Dr Slater has pioneered this approach, since people seem to react to virtual reality as they do to real life, but no one gets hurt and conditions can be controlled precisely. Because the participants know it is not real, many of the ethical obstacles to placing them in such situations are removed. But Dr Slater proved the tool’s usefulness in 2006, when he used it to recreate a famous experiment conducted in the 1960s by Stanley Milgram, an American psychologist. Milgram showed that ordinary people would obey orders to the point of delivering potentially lethal electric shocks to strangers—an experiment that, even though nobody really received any shocks, would be ruled out today, on ethical grounds. Dr Slater’s volunteers behaved similarly to Milgram’s.

Virtual reality may thus allow Dr Levine to understand the collective choreography of violence better than he does now, but he is already convinced that, despite the moral panic over violence in Britain today, the influence of groups is largely benign. His work could have practical consequences, since police generally aim to break crowds up. If he is right, that approach may unintentionally lead to more fights. It sounds counter-intuitive, but many of the best ideas are. And if it is true, then perhaps Big Brother could give up the CCTV habit and go and do something more useful instead.

Social networks

Primates on Facebook

Feb 26th 2009 | SAN FRANCISCO
From The Economist print edition

Even online, the neocortex is the limit

THAT Facebook, Twitter and other online social networks will increase the size of human social groups is an obvious hypothesis, given that they reduce a lot of the friction and cost involved in keeping in touch with other people. Once you join and gather your "friends" online, you can share in their lives as recorded by photographs, "status updates" and other titbits, and, with your permission, they can share in yours. Additional friends are free, so why not say the more the merrier?

But perhaps additional friends are not free. Primatologists call at least some of the things that happen on social networks "grooming". In the wild, grooming is time-consuming and here computerisation certainly helps. But keeping track of who to groom—and why—demands quite a bit of mental computation. You need to remember who is allied with, hostile to, or lusts after whom, and act accordingly. Several years ago, therefore, Robin Dunbar, an anthropologist who now works at Oxford University, concluded that the cognitive power of the brain limits the size of the social network that an individual of any given species can develop. Extrapolating from the brain sizes and social networks of apes, Dr Dunbar suggested that the size of the human brain allows stable networks of about 148. Rounded to 150, this has become famous as "the Dunbar number".

Many institutions, from neolithic villages to the maniples of the Roman army, seem to be organised around the Dunbar number. Because everybody knows everybody else, such groups can run with a minimum of bureaucracy. But that does not prove Dr Dunbar's hypothesis is correct, and other anthropologists, such as Russell Bernard and Peter Killworth, have come up with estimates of almost double the Dunbar number for the upper limit of human groups. Moreover, sociologists also distinguish between a person's wider network, as described by the Dunbar number or something similar, and his social "core". Peter Marsden, of Harvard University, found that Americans, even if they socialise a lot, tend to have only a handful of individuals with whom they "can discuss important matters". A subsequent study found, to widespread concern, that this number is on a downward trend.

The rise of online social networks, with their troves of data, might shed some light on these matters. So *The Economist* asked Cameron Marlow, the "in-house sociologist" at Facebook, to crunch some numbers. Dr Marlow found that the average number of "friends" in a Facebook network is 120, consistent with Dr Dunbar's hypothesis, and that women tend to have somewhat more than men. But the range is large, and some people have networks numbering more than 500, so the hypothesis cannot yet be regarded as proven.

What also struck Dr Marlow, however, was that the number of people on an individual's friend list with whom he (or she) frequently interacts is remarkably small and stable. The more "active" or intimate the interaction, the smaller and more stable the group.

Thus an average man—one with 120 friends—generally responds to the postings of only seven of those friends by leaving comments on the posting individual's photos, status messages or "wall". An average woman is slightly more sociable, responding to ten. When it comes to two-way communication such as e-mails or chats, the average man interacts with only four people and the average woman with six. Among those Facebook users with 500 friends, these numbers are somewhat higher, but not hugely so. Men leave comments for 17 friends, women for 26. Men communicate with ten, women with 16.

What mainly goes up, therefore, is not the core network but the number of casual contacts that people track more passively. This corroborates Dr Marsden's ideas about core networks, since even those Facebook users with the most friends communicate only with a relatively small number of them.

Put differently, people who are members of online social networks are not so much "networking" as they are "broadcasting their lives to an outer tier of acquaintances who aren't necessarily inside the Dunbar circle," says Lee Rainie, the director of the Pew Internet & American Life Project, a polling organisation.

Humans may be advertising themselves more efficiently. But they still have the same small circles of intimacy as ever.

Greenhouse gases

OCOck up

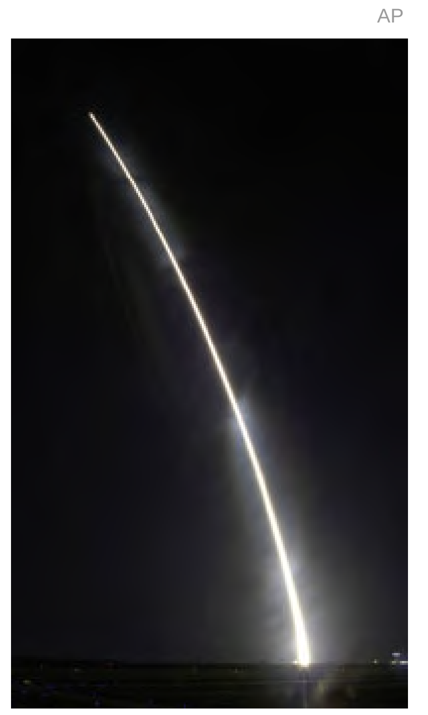
Feb 26th 2009
From The Economist print edition

America's new carbon-dioxide-monitoring satellite crashes soon after launch

ATTEMPTS to understand more about the Earth's atmosphere and the effects on it of increasing levels of carbon dioxide suffered a blow on February 24th. A shroud protecting the *Orbiting Carbon Observatory* (OCO), an American satellite intended to monitor levels of the gas, failed to detach as it was being carried into space. Instead of going into orbit, the Taurus rocket carrying the craft crashed into the sea near Antarctica.

The OCO, which cost $278m and took eight years to develop, would have been the first American satellite dedicated to the study of atmospheric carbon dioxide. It was supposed to join five others in a formation known as the "A-train". The plan was for OCO's measurements to be synchronised with an analysis of ozone, nitrogen dioxide, methane and other greenhouse gases by the rest of the fleet. One of these satellites, *Aura*, does already look at carbon dioxide, but its measurements are confined to the upper atmosphere. The instruments on OCO would have examined the lower atmosphere, and in finer detail.

AP



When the rockets go up…

What the researchers were trying to discover were the places on Earth where carbon dioxide is being added to the atmosphere and those where it is being removed. Including man-made emissions, the Earth's "carbon cycle" releases about 330 billion tonnes of the gas each year. Most of this is then absorbed by so-called carbon sinks, a mixture of photosynthesising plants and chemical precipitation, while a small amount remains to contribute to the rise in carbon-dioxide concentration that has been going on for the past 150 years. About half of the sunk carbon is absorbed by oceans, but exactly where the rest goes—and in what quantities—is not well understood. Remote habitats such as rainforests are clearly involved, but the lack of instruments in these places means the details are hazy.

Michael Freilich, the director of the Earth Science Division of NASA, America's space agency, says his team will look at how other measurements taken by the A-train might be used to compensate for the loss of OCO, and how these measurements can be co-ordinated with data from other sources. Such sources could include *Ibuki*, a satellite dedicated to monitoring carbon dioxide and methane, which was launched by the Japanese space agency in January. So the loss of OCO is a setback to understanding the details of global warming, but thanks to Japan, perhaps not a complete disaster.

Psychology

Sunny side up

Feb 26th 2009
From The Economist print edition

Optimism, it seems, is in the genes

FOR some people in this world, the glass always seems to be half-full. For others it is half-empty. But how someone comes to have a sunny disposition in the first place is an interesting question.

It has been known for a long time that optimists see the world selectively, mentally processing positive things while ignoring negative ones, and that this outlook helps determine their health and well-being. In recent years, it has also become clear that carriers of a particular version of a particular gene are at higher risk than others of depression and attempted suicide when they face traumatic events. The gene in question lies in a region of the genome that promotes the activity of a second gene, which encodes a protein called the serotonin transporter. Serotonin is a messenger molecule that carries signals between nerve cells, and it is known to modulate many aspects of human behaviour, although the details are complex and controversial. The transporter protein recycles serotonin back into the cell that produced it, making it available for reuse, but also reducing the amount in the junctions between cells and thus, it is presumed, the strength of the signal.

It has looked increasingly likely, therefore, that genes—particularly those connected with serotonin—have a role to play in shaping a person's outlook. So Elaine Fox and her colleagues at the University of Essex, in Britain, wondered whether genes play a part in the selective attention to positive or negative material, with consequent effects on outlook.

To find out, they took samples of DNA from about 100 people and then subjected these people to what is known as the dot-probe paradigm test to see how they reacted to different stimuli. In this test participants are briefly shown photographs that may be positive, negative or neutral in tone. They then have to press a keypad to indicate when a dot has appeared on the screen. It has been found by experience that the more distracting an image is, the longer a person takes to respond when the dot appears. That allowed Dr Fox and her team to discover how distracting particular people found particular images.

In a paper just published in the *Proceedings of the Royal Society B* they report that, sure enough, gene-related variation caused a bias in attention towards positive and negative material. Some people had two "long" versions of the promoter gene (one inherited from each parent), a combination that reduces the amount of serotonin in the junctions between nerve cells. These individuals were biased towards positive images and away from negative ones. By contrast, those who had either a long and a short version of the gene, or two short versions (and thus, presumably, more serotonin in the junctions), did not have such protective biases. In other words, the optimists really did see the world differently.

Rose-tinted spectacles may be good for one's health, as these results fit in with wider ideas about how a tendency to look on the bright side of life is part of being resilient to stress. Those with short variants of this gene are expected to have an increased susceptibility to mood disorders following such stress. It is not all good news, though, for optimists. Because these results suggest that a person's attitude to life is inherited, they serve as a stark warning to all buoyant optimists that trying to cheer the rest of the world up with nothing more than a smile and an effortlessly sunny disposition is doomed to failure.

Homo erectus

A footprint in the sands of time

Feb 26th 2009
From The Economist print edition

Homo erectus had a manly gait

Science



THIS footprint is part of one of two series of fossil tracks found recently in Kenya in rocks that are 1.5m years old. It is thought to have been made by *Homo erectus*, an ancestor of modern *Homo sapiens*. As the name suggests, *Homo erectus* is known from its skeleton to have walked upright, but the details of its gait could, in the past, be inferred only from bones, rather than being studied more directly. The new tracks, reported in *Science* by Matthew Bennett of Bournemouth University, in Britain, and his colleagues, confirm that *Homo erectus* walked heel-to-toe as a modern human does, rather than with the ape-like gait of its own ancestors, the australopithecines.

Economist.com BOOKS & ARTS

Corruption in Kenya

How to ruin a country

Feb 26th 2009
From The Economist print edition

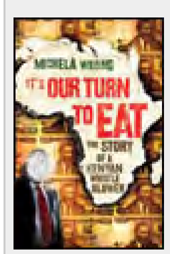
Eyevine



John Githongo (shown below) fought the corruption that is destroying Kenya but was defeated

THIS is the tale of the tragic failure of a brave and honest man appointed to expose corruption by a new Kenyan president who came to power on a wave of high-minded enthusiasm in late 2002, claiming to be a clean-handed reformer. Within a few years the brave man, John Githongo, is betrayed by the president, Mwai Kibaki, and by most of the big man's closest colleagues, many of whom prove themselves to be patently corrupt. Mr Githongo is at first intensely loyal to Mr Kibaki, who gives him an office down the corridor in State House. But the whistleblower comes to realise that the president acquiesces in corruption of the grossest kind, and flees for his life into exile.

It's Our Turn to Eat: The Story of a Kenyan Whistleblower
By Michela Wrong



Fourth Estate; 400 pages; £12.99. To be published in America by Harper in June

There is far more to this gripping saga than that. It is a down-to-earth yet sophisticated exposé of how an entire country can be munched in the clammy claws of corruption. It is also a devastating account of how corruption and tribalism—the author prefers the grander term ethno-nationalism—reinforce each other, as clannish elites exploit collective feelings of jealousy or superiority in an effort to ensure that their lot wins a fat, or the fattest, share of the cake. Hence the book's title: "It's our turn to eat".

Mr Githongo, who reported for *The Economist* (among other journals) in the 1990s, is portrayed by the author, an outstanding former *Financial Times* journalist, to whose house in London he fled, as a complex character: jovial, moody, dogged, ingenious and understandably obsessive. Through his prism, the author describes Kenya's history over the past two decades, "probing the roots of a dysfunctional African nation".

After independence in 1963, Jomo Kenyatta and his mainly Kikuyu inner circle steadily plundered the country, ensuring that their fellow Kikuyus and closely related Meru and Embu groups, together comprising some 28% of Kenya's people, acquired an ever-larger slice of the land. After his death in

1978, his successor, Daniel arap Moi, who hailed from the much smaller Kalenjin-speaking group of tribes, reckoned it was their turn to eat—and how. Eventually, in 2002, in what looked like a pan-ethnic revolt against Mr Moi's lot, Mr Kibaki, another Kikuyu, won a multiparty election amid hopes that Kenya would at last have a decent, reasonably clean administration in which merit rather than tribe would be the way to advancement. Mr Githongo's appointment as the government's anti-corruption tsar was hailed as a happy sign of intent.

No such luck. Mr Githongo almost immediately spotted a massive scam, to be known after a murky company called Anglo-Leasing, that creamed off some $750m mainly by overbilling the state—with ministerial connivance—in some 18 projects. He noted that more than half of these scams had originated in Mr Moi's era but had deftly been carried over into the new and supposedly clean one. It soon became clear that not only were some of the most senior ministers in the government involved but also that the president was unwilling to do anything about it.

Moreover, as Mr Githongo made secret tapes of conversations with these villains, two more things became equally clear. The main perpetrators, bound by a tight code of ethnic solidarity, flagrantly appealed to him, as a fellow Kikuyu, to be loyal to his tribe. He also realised, even after he had fled into exile, that this so-called "Mount Kenya Mafia" was determined to use some of its ill-gotten gains to fill its party's coffers in an effort to win the general and presidential elections due at the end of 2007. This group would stop at nothing to hold on to power.

In the event, when it seemed that Raila Odinga, the populist presidential candidate whose campaign was full of anti-Kikuyu innuendo, was winning the race in late 2007, the old guard around Mr Kibaki set about fiddling the result, prompting riots and ethnic massacres around the country in which some 1,500 perished and at least 300,000 were displaced. After two months of turmoil and political paralysis, a shabby and unwieldy compromise was reached under the aegis of the UN's former secretary-general, Kofi Annan, whereby Mr Kibaki held on to the presidency while Mr Odinga became prime minister.

Kenya, meanwhile, had been torn apart as never before. Mr Odinga, like President Barack Obama's father, is a Luo, Kenya's third-most-populous group, which fiercely considered that it was its "turn to eat". It had grievously missed out under two Kikuyu-dominated administrations and under Mr Moi's Kalenjin one.

One of the most disturbing aspects of the book is the dismal performance both of the World Bank and of Britain's Department for International Development (DFID). The bank has been indulgent towards Kenya's leaders and inept when it tried to do something about their corruption. There was a "dangerous cosiness" between the bank and Kenya's government.

For the current British government, the book is even more disturbing. A flagship of Tony Blair's New Labour, DFID was a new ministry no longer subordinate, as its predecessors had been, to the Foreign Office. It disbursed cash for aid far more abundantly than ever before and with fewer strings, betokening a determination to "end poverty". As Michela Wrong puts it, the amount of money which it disbursed became "the only solid yardstick of progress, hardly a situation likely to encourage discrimination amongst officials responsible for approving projects". When Britain's then high commissioner to Kenya, Sir Edward Clay, one of a small band of righteous heroes in the book, spoke out courageously against corruption, his DFID counterparts did their best to undermine him.

A year after the corrupt election fiasco of late 2007 and early 2008, nothing fundamentally has changed. Almost all the top ministers and civil servants fingered by Mr Githongo are still in office; so is Mr Kibaki. Even if Mr Odinga were president, as the majority of voters almost certainly intended him to be, few Kenya-watchers would be confident that the basics would have changed, except that a new elite would be "eating" better. The mixture of greed and ethnic exploitation is as potent and combustible as ever: a sorry state of affairs.

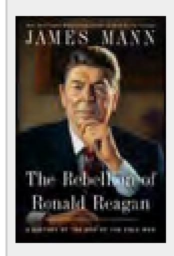
It's Our Turn to Eat: The Story of a Kenyan Whistleblower.
By Michela Wrong.
Fourth Estate; 400 pages; £12.99. To be published in America by Harper in June

The end of the cold war

Reagan's rebellion

Feb 26th 2009
From The Economist print edition

The Rebellion of Ronald Reagan: A History of the End of the Cold War
By James Mann



Viking; 396 pages; $27.95. To be published in Britain by Penguin in July

Buy it at
Amazon.com
Amazon.co.uk

JAMES MANN, whose speciality is the murky world of Republican policymaking, and whose 2004 book on George Bush's war cabinet, "Rise of the Vulcans", was a deserved hit, has produced a winner again. His subject is Ronald Reagan, his relationship with Mikhail Gorbachev and the ending of the cold war. Backed by a thorough trawl of American documents and people (though lacking corresponding access to Russian sources), it is a sound account, well worth reading.

He kicks off with a chapter on the relationship between Reagan and Richard Nixon, who may have kept a low public profile but bombarded the president with advice. And this advice appears with hindsight to have been fairly bad. Along with Henry Kissinger, who also periodically weighed in, Nixon seemed unable to grasp what Reagan instinctively understood, even if he was wary about articulating it: that Mr Gorbachev really was a different kind of Soviet leader from those that America had faced in the previous decades.

It is this, according to Mr Mann, that made Reagan a rebel, and his rebellion was rooted in a profound philosophical difference. One realist school of thought held that the cold war was something immutable, a fact of history that could at best be managed through the grinding diplomatic protocols known as detente. The other school, to which Reagan belonged, sensed that communism was weaker than it looked and that the cold war would die with it.

Unfortunately, it was not just Nixon and Mr Kissinger who belonged to the first realist school but also most of the State Department, the Pentagon and the rest of the national security apparatus, not to mention the whole chorus of the conservative commentariat. Here, for instance, is George Will, of the *Washington Post*, writing in 1987: "Reagan seems to accept the core of the catechism of the anti-nuclear left…the notion that the threat is the existence of nuclear weapons, not the nature of the Soviet regime." In extending a hand of friendship to Mr Gorbachev, Reagan terrified the great bulk of his own political base.

AP

But how did Reagan, who had never been to the Soviet Union, and who first came to politics (in those days, Mr Mann reminds us, as a Democrat) battling against labour unions and alleged communist subversion in the film industry, come to feel this? Mr Mann's exploration of this puzzle revolves around the president's extraordinary (though entirely above-board) relationship with a semi-academic, Suzanne Massie, the author of a rather fanciful book about Russian culture called "Land of the Firebird". For an unofficial adviser, with no job or proper function, Ms Massie held a remarkable 20 or so meetings with the president, and they wrote frequently to one another. As Mr Mann shows, she carried back-channel messages between Reagan and the Kremlin. And she gave the president his favourite catch-phrase for dealing with Russians: "Trust, but verify."

Other parts of the book deal, in great detail, with the genesis of Reagan's 1987 appeal to Mr Gorbachev to "tear down this wall!", delivered at the Brandenburg Gate within sharp-shooter range of East Berlin's *Volkspolizei*. Even as Reagan was travelling to Germany, nervous detentist elements in his own government were trying to rewrite his speech. And there is an excellent final section on the summit diplomacy that did so much to change Western perceptions of the Soviet Union.

The book, fascinating and recommended though it is, does leave some

large questions unanswered. It says nothing beyond, literally, a sentence, about the importance of America's covert war in Afghanistan in pressuring the Soviet Union into defeat. And although it lays out Reagan's fundamentally optimistic view of Mr Gorbachev, and indeed of history, it does not come to any firm conclusion as to how consequential this actually was. After all, the concessions, on arms control and so much else, all came from the Russian side.

Ultimately, or so Mr Mann concludes, the Soviet Union collapsed because of Mr Gorbachev and the communist system's internal contradictions. Neither the arms race nor any concerted effort to strangle the Soviet economy pushed the empire over the edge. Nor, for that matter, did Reagan's sensible policy of conditional engagement. Which does rather raise the question: how much in the end did that rebellion of Ronald Reagan really matter?

The Rebellion of Ronald Reagan: A History of the End of the Cold War.
By James Mann.
Viking; 396 pages; $27.95. To be published in Britain by Penguin in July



My buddy, Ronnie

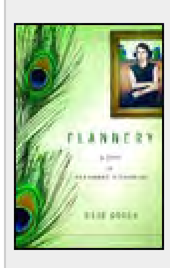
The life of Flannery O'Connor

All beak and claws

Feb 26th 2009
From The Economist print edition

"THIS is one of the greatest stories ever written in the United States," suggested Robert Giroux, a distinguished American publisher, after reading the manuscript of "A Good Man is Hard to Find" by Flannery O'Connor. "That's good stuff," echoed her fellow-southerner, William Faulkner, about O'Connor's first novel, "Wise Blood". Others found her acidly comic tales strong meat. Asked to provide a puff for "Wise Blood", Evelyn Waugh, a British novelist, was moved to ponder: "Why are so many characters in recent American fiction sub-human?" *Time* magazine, in summarising her cast of drowning boys, garrulous southern grandmothers and man-killer prophets, called them "God-intoxicated Hillbillies".

Flannery: A Life of Flannery O'Connor
By Brad Gooch



Little, Brown; 448 pages; $30. To be published in Britain by Little, Brown in April

Buy it at
Amazon.com
Amazon.co.uk

O'Connor is an intriguing writer; each year her status as "minor" is adjusted upward. When she died in 1964, aged 39, of lupus, she had written 31 stories, two novels and, aside from a three-week trip to Europe to visit Lourdes, had spent her entire life in the United States, the bulk of it on her mother's dairy farm in central Georgia. "There won't be any biographies of me", she maintained, "because, for only one reason, lives spent between the house and the chicken yard do not make exciting copy." In 1955 she submitted to a rare television interview with NBC and proved a publicist's nightmare, refusing to answer personal questions.

AP

Birds were her delight

Until now her life has remained hidden behind the hard surface of her fiction. One of the strengths of Brad Gooch's biography is its elegant pooh-poohing of her claim that "experience is the greatest deterrent to fiction" and that "any story in which I reveal myself in completely will be a bad story." In fact, her constricted view of the world was integral to her artistic vision.

Like Waugh, O'Connor was an accomplished cartoonist at college, signing her drawings with a chicken logo. Birds were her chief delight: the peacocks and bantams that she walked around her yard, and for which she even sewed underwear. Sheltered, plain, shy, she preferred feathered creatures to people and identified with them; underneath she was all beak and claws. Her father was diagnosed with lupus when she was 12 and in many respects she remained stuck at that age, looking out at the world with a childlike detachment and not letting anyone in, except God. A Roman Catholic, she wrote about grotesques, she explained, to convey the shocking Christian vision of original sin. Not much sin coloured her life. Mr Gooch, an indefatigable and poker-faced researcher, tracks down the one man known to have kissed her: "I had the feeling of kissing a skeleton and in that sense it was a shocking experience."

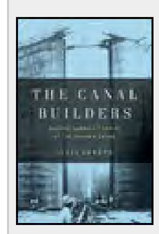
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American canal building

Waterway triumphs

Feb 26th 2009
From The Economist print edition

Bond of Union: Building the Erie Canal and the American Empire
By Gerard Koeppel



Da Capo Press; 480 pages; $27.95 and £16.99

Buy it at
Amazon.com
Amazon.co.uk

AS SOME governments are about to rediscover, the actual construction work can be the easy part when embarking on large infrastructure projects. Winning the necessary political support is much harder, especially from legislators keen on alternative public works that more directly benefit their constituents. The competing interests of places that stand to lose or gain from projects are further obstacles to overcome. So are the difficulties contractors experience when they seek to recruit thousands of dependable employees willing to work long hours in arduous conditions.

Just how stressful it is to get these projects started, let alone completed, is spelt out in case studies of America's two proudest achievements in canal building. Gerard Koeppel, a journalist, shows a scholarly fascination for the precise details of the legislative progress of the Erie Canal, the waterway that, in 1825, joined the Great Lakes to the Hudson river and so to the Atlantic ocean at New York City. Julie Greene, a historian, takes a more journalistic approach as she tells the sometimes joyful but more often pitiful stories of the builders of the Panama Canal, which, in 1914, joined the Pacific and Atlantic oceans.

The commercial success of both canals exceeded the most extravagant expectations of their backers. The Erie Canal enabled the United States to penetrate the Appalachian range before the French and British could lay permanent claim to the continental interior. The Panama Canal halved the shipping distance between New York and San Francisco and opened up Asian markets to the United States.

Politicking nonetheless bedevilled the Erie Canal from its conception in 1807 to its completion 18 years later. A slew of presidents from Virginia were cool to a project that boosted the commercial strength of New York. Thomas Jefferson wanted waterworks to increase shipping on the Potomac river and dismissed the proposed canal as "little short of madness".

The imperial mood of the times and the boisterous backing of Presidents Theodore Roosevelt and William Taft provided all the political support the Panama Canal needed to secure federal funding. Diplomatic spats were solvable. The government of Panama was sometimes obstreperous but ultimately bent to American muscle. Manpower was the real problem, and in particular the difficulty of persuading engineers and skilled tradesmen to leave the United States to dig a ditch in a fetid tropical swamp.

Most of these mainly white Americans commanded far better pay and conditions than even skilled workers recruited in Central America and the Caribbean. The agency responsible for building the canal and administering the Canal Zone, the Isthmian Canal Commission (ICC), had no alternative but to provide them with such American necessities as iceboxes and porcelain baths as well as such perks as home leave and houses with wide verandas. The privileged status of the Americans caused understandable resentment among workers from elsewhere but the efforts of trade unionists to organise these workers were frustrated by their diversity. The ICC had, of necessity, to recruit widely to hire the 57,000 people it needed and this, it noted, had one beneficial result: the many different races and nationalities minimised the chances of "the combination" of the workforce "which would be disastrous".

The chastened political left sought solace in the thought that the Panama and Erie canals were fine advertisements for state enterprise. Their very success demonstrated that public projects were not necessarily inefficient, extravagant and dishonest. Today's free-spending governments may take heart.

Bond of Union: Building the Erie Canal and the American Empire.
By Gerard Koeppel.
Da Capo Press; 480 pages; $27.95 and £16.99

Social inequality

Always with us?

Feb 26th 2009
From The Economist print edition

The Spirit Level: Why More Equal Societies Almost Always Do Better
By Richard Wilkinson and Kate Pickett



Allen Lane; 297 pages; £20

Buy it at
Amazon.com
Amazon.co.uk

SOME men steal out of need or avarice; others kill themselves out of despair, or murder for revenge or gain. These episodes in individual tales display such striking regularities in aggregate that some of the social scientists who first applied the rules of probability to human affairs questioned the very notion of free will. “Society prepares the crime,” wrote Adolphe Quetelet, a Belgian statistician, in 1835, “and the guilty person is only the instrument.”

The findings of those statisticians’ successors—that poor children are more likely to fail at school, poor adults to commit crimes and die young, and so on—are nowadays uncontroversial. And policymakers mostly eschew metaphysics. Instead, they try to break such links by spending to “end child poverty” and by targeting health and education initiatives on the neediest. Yet such attempts are doomed to disappoint, say British social scientists, Richard Wilkinson and Kate Pickett, because they conceive of each social ill in isolation, rather than treating their shared root cause. Moreover, they misidentify that cause: it is not poverty as such, but inequality.

It is a sweeping claim, yet the evidence, here painstakingly marshalled, is hard to dispute. Within the rich world, where destitution is rare, countries where incomes are more evenly distributed have longer-lived citizens and lower rates of obesity, delinquency, depression and teenage pregnancy than richer countries where wealth is more concentrated. Studies of British civil servants find that senior ones enjoy better health than their immediate subordinates, who in turn do better than those further down the ladder.

And the evidence is that the differences in status cause these “gradients”. Low-caste Indian children do worse on cognitive tests if they must state their identities beforehand. High-status baboons bred in captivity show elevated levels of stress hormones and become ill more often when they are moved to groups where they no longer dominate.

What to do about this sickness caused by other people’s wealth? Swingeing taxes on the rich, or smaller differences in pay in the first place, say the authors, citing Sweden and Japan as instances of the two alternatives. A decade ago even left-wing politicians were “intensely relaxed about people getting filthy rich”. Now, as it becomes clearer that some of the rich got that way by theft, the idea that they have also caused injury more subtly will gain a readier hearing.

Too ready, perhaps: what if the price of greater equality is lower growth? The received wisdom—admittedly looking a little threadbare right now—is that rich rewards are necessary to stimulate the innovation on which growth depends. No loss, say the authors: “We have got close to the end of what economic growth can do for us.” But that is a claim that needs to be supported, rather than simply made in a few sentences. If our ancestors had declared themselves thus satisfied, we would be without many things that we value—and that they would have valued too, could they have imagined them. Should we be ready to dismiss joys we have never known?

The Spirit Level: Why More Equal Societies Almost Always Do Better.
By Richard Wilkinson and Kate Pickett.
Allen Lane; 297 pages; £20

Krishna exhibition

Seduced by a flute

Feb 26th 2009
From The Economist print edition

The enchantment of Krishna revealed in textiles at London's Asia House

AN EXHIBITION does not have to be a blockbuster to be a knock-out. "Krishna & Devotion: Temple Hangings from Western India", at Asia House until April 4th, shows only 40 works, none of them world famous. But it is a jewel. The main exhibits are the surprisingly large textile wall hangings, most of them vivacious painted cottons, although some are embroidered and block-printed or woven silk brocade. There are also miniature paintings and a single, twinkling turban ornament. Everything relates to the worship of the Hindu god Krishna when he was a young cowherd. He was mischievous and musical, a playful, seductive, much indulged youth. Members of the *pushti marg* sect, who commissioned these works, adore him for it all.

"These painted hangings are unique both as an art form and as an adjunct to devotional worship," writes Robert Skelton, a former keeper of the Indian section of the Victoria and Albert Museum, in the catalogue. They were made as adornments, expressions of faith—and to create a mood. This is the first time they have been shown in Britain though an exhibition toured America between 1973 and 1976. There are keen collectors: loans to London have come from India, Europe and America.

The cloths are called *pichhvais*, "that which hangs at the back". They were, and still are, hung behind the venerated stone statue of young Krishna at the sect's centre of worship in Nathdwara, Rajasthan—though, in fact, *pichhvais* hang wherever the sect worships. They were made in sets and changed according to the cycle of festivals and seasons, and also the times of day. The examples at Asia House date from the 18th to the 20th centuries.

The show opens with a bold, forceful young Krishna, his left hand raised high above his head (see picture). This symbolises his feat in lifting Mount Govardhan and holding it, as if it were a giant umbrella, over a nearby village to protect it from the wrath of Indra, the god of war and weather. (He had proposed that the villagers give their offerings not to Indra but to the mountain because, for their cows, grazing land was more important than rain. Indra capitulated.) Krishna is dressed magnificently, draped with so many strings of pearls and lotus buds that they form a floor-length apron. The god's supremacy established, the visitor moves on to see some of his more lighthearted adventures.

Courtesy of Francesca Galloway



Krishna, the protector

One of the most charming hangings is an autumn cloth. Here the young god stands under a tree playing his flute. So many cows are irresistibly drawn by the music that they seem to fill every inch of space. It was not only cows who were seduced. The most romantic hanging is a summer view of Krishna and his consort Radha embracing. Dressed in filmy garments, they stand in the centre of a turquoise sea dotted with deep pink lotuses and lime-green leaves. Butterflies flit across the water; bees dart. One can almost feel the steamy heat, not only of the ambient sort.

These are lively, sometimes lyrical, sometimes startlingly beautiful works of art. In their company, spirits rise—an antidote for the recession blues.



PEOPLE

OBITUARY

Christopher Nolan

Feb 26th 2009
From The Economist print edition

Christopher Nolan, the voice of the crippled, died on February 20th, aged 43

Writer Pictures



YOU wouldn't have wanted to be Christy Nolan. His two arms looked normal, but they would fly out randomly, like a clockwork doll's. "Dreadful deadly spasms" of cerebral palsy shot their way from his cranium to his spine and into his feet. He needed carrying to the bath, to the toilet, to bed; his long legs were good for nothing, collapsing under him like a deck of cards. When he tried to talk, nothing came out but "dull looks, dribbles and senseless sounds". He could not even wipe the saliva from his own face.

In bed at night, when he was as able-bodied as anyone, he would rehearse what his "drunken, drooling body" could do, and what it couldn't:

> Can't chew, can't swallow, so why chew? Can't call—can call, a famished moan maybe yet it suffices...can't cry—can cry, can cry, can cry wet pillows full but who cares...can't laugh—can laugh, can can can

At birth, at the County Hospital at Mullingar in Ireland, he had been deprived of oxygen for two hours. He should have died, but instead "sagaciously he dolefully held on". People pitied him, stroked his head and said God was good, but even as a boy he was not so sure. The "closeted cossetted certainty of Christ" could always calm him, as could communion when Father Flynn was able to sneak the host between his spasming, locking jaws. But once, in St John the Baptist's, he had himself wheeled to the life-size crucifix with its grey bloodied face and threw out his left arm in a great arc to give Christ two fingers, because he was to blame.

And yet, despite it all, he could use words. At the age of 13, he could write this:

> Among firs, a cone high-flown,
> Winged, popped,
> Hied, foraying, embalming,
> Sembling tomb
> Among coy, conged fir needles,
> A migratory off-spring

> Embarks on life's green film.

For a long time, no one knew. He could communicate: yes with upshot eyes, a neck-bow for affirmation, a drubbing of feet on his wheelchair for attention. The IQ tests always went well, well enough for him to go to "ordinary" school at Mount Temple in Dublin. His blue eyes blazed with intelligence. But no one suspected that in his head were stored millions of words, "nutshelled" and ready. They included all the songs and stories he had heard from his father, the poems recited by his teachers, the alphabet-words stuck up round the kitchen by his mother, glittering fragments of Hopkins and Joyce and Yeats. His overriding ambition was how to "best his body" and get them out.

At the age of 11 he learned how. With a rubber-tipped stick strapped like a unicorn's horn to his forehead, and dosed with a new pill that calmed his neck muscles a little, he picked out one letter, then another, on a typewriter, "by a bent, nursed, and crudely given nod of his stubborn head":

> His own mother cradled his head but he mentally gadded here and there in fields of swishing grass and pursed wildness. His mind was darting under beech copper-mulled, along streams calling out his name, he hised and frolicked but his mother called it spasms. Delirious with the words plopping onto his path he made youth reel where youth was meant to stagnate. Such were [his] powers as he gimleted his words onto white sheets of life.

Sometimes one word would take 15 minutes to write. It never got faster; his last work, "The Banyan Tree", a novel based on his family's farming history in Westmeath, took a decade. But as soon as he began to get the "beautiful words" on paper, he won competitions. Weidenfeld & Nicholson published his poems and writings when he was 15. The book was called "Dam-Burst of Dreams", as it was. He could speak, and not just for himself, but for all the other, silent, damaged boys of the world.

Insults ran off him. Forgetfulness, he wrote, "fugues tongues and balms words". He called himself a cripple unsparingly in his autobiography, "Under the Eye of the Clock", which won the 1988 Whitbread Book of the Year. Some said disability got the prize for him, but what won it was the language, uncorralled and fresh as though the words had never been tried before. He made words do everything his body could not. Among his favourites were "frolicking" and "rollicking"; "hollyberries", meaning compensations among the sharp things of life; and "crested", meaning glorious, as though he lifted his head to say it.

Nothing could have happened without his parents. To the end, his mother gripped his chin as he wrote. They carried him on their shoulders, held him, one on each side, to let him ride a pony, steadied him in a stream to feel the icy water on the rocks beneath his feet. His mother had told him, when he was three and crying with frustration, that she liked him just as he was. From that point, "he [fanned] the only spark he saw, his being alive".

Once, on holiday on the Burren, his family buried him standing up in sand, just his head and shoulders showing. He knew then what it felt like to be able-bodied and straight. But his head was at the level of people's feet; so he asked to be returned to his wheelchair. He might loll and flop in it, "zoo-caged" as he was. But it was also his proud podium and his throne.

Overview

Feb 26th 2009
From The Economist print edition

Consumer prices in **America** rose by 0.3% in January after having fallen in each of the previous three months. Energy prices rose for the first time since July, but were still nearly a third below their peak. American house prices continued to fall. The S&P/Case-Shiller index of home prices in 20 big cities was down by 18.5% in the year to December. Despite this, sales of previously owned homes fell by 5.3% in January.

Japan's exports on a customs basis plunged, leaving them 45.7% lower in the year to January. In that time exports to America plunged by a staggering 52.9%. Shipments to Europe were hit nearly as hard, falling by 47.4%. The country's trade deficit continued to widen, reaching $9.9 billion, despite a sharp fall in imports.

Business confidence fell again in **Germany**. The closely watched Ifo index dropped in February, after a slight rise in the previous month. Orders for industrial goods in the **euro area** fell by 5.2% in December, the fifth consecutive monthly decline.

Poland's central bank cut its main interest rate by a quarter of a percentage point, to 4%, on February 25th.

Standard & Poor's, a rating agency, cut **Ukraine's** long-term foreign-currency rating to CCC+, the lowest in Europe.

Thailand's central bank cut its benchmark interest rate by half a percentage point, to 1.5%, the third reduction in as many months.



Output, prices and jobs

Feb 26th 2009
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2008†	2009†	latest	latest	year ago	2008†	rate‡, %
United States	−0.2 Q4	−3.8	+1.2	−2.0	−10.0 Jan	nil Jan	+4.3	+3.8	7.6 Jan
Japan	−4.6 Q4	−12.7	−0.2	−3.2	−20.8 Dec	+0.4 Dec	+0.7	+1.4	4.4 Dec
China	+6.8 Q4	na	+9.0	+6.0	+5.7 Dec	+1.0 Jan	+7.1	+5.9	9.0 2008
Britain	−1.9 Q4	−6.0	+0.7	−2.6	−9.3 Dec	+3.0 Jan§	+2.2	+3.6	6.3 Dec††
Canada	+0.5 Q3	+1.3	+0.5	−0.7	−5.1 Nov	+1.1 Jan	+2.2	+2.4	7.2 Jan
Euro area	−1.2 Q4	−5.7	+0.8	−2.1	−12.0 Dec	+1.1 Jan	+3.2	+3.1	8.0 Dec
Austria	+0.5 Q4	−0.8	+1.4	−1.3	+0.7 Nov	+1.3 Dec	+3.6	+3.2	3.9 Dec
Belgium	−0.5 Q4	−5.2	+1.3	−1.3	−11.6 Nov	+2.3 Jan	+3.5	+4.5	11.1 Jan‡‡
France	−1.0 Q4	−4.6	+0.7	−1.7	−11.1 Dec	+0.7 Jan	+2.8	+2.8	8.1 Dec
Germany	−1.7 Q4	−8.2	+1.1	−2.5	−12.0 Dec	+0.9 Jan	+2.8	+2.6	7.9 Feb
Greece	+2.6 Q4	+0.7	+1.1	−1.8	−8.7 Dec	+1.8 Jan	+3.9	+4.1	7.4 Oct
Italy	−2.6 Q4	−7.1	−0.6	−2.3	−14.3 Dec	+1.6 Jan	+3.0	+3.3	6.7 Q3
Netherlands	−0.6 Q4	−3.4	+1.8	−1.6	−13.3 Dec	+1.9 Jan	+2.0	+2.3	3.9 Jan††
Spain	−0.7 Q4	−3.8	+1.1	−2.3	−15.4 Dec	+0.8 Jan	+4.3	+3.9	14.4 Dec
Czech Republic	+1.0 Q4	−2.4	+4.0	−1.4	−14.6 Dec	+2.2 Jan	+7.5	+6.3	6.8 Jan
Denmark	−1.2 Q3	−1.9	−0.6	−1.7	−5.4 Dec	+1.8 Jan	+2.9	+3.5	2.3 Jan
Hungary	+0.8 Q3	−0.3	+0.4	−3.0	−23.3 Dec	+3.1 Jan	+7.1	+6.1	8.0 Dec††
Norway	+0.8 Q4	+5.6	+1.5	−1.0	+3.7 Dec	+2.2 Jan	+3.7	+3.8	3.0 Dec***
Poland	+4.8 Q3	na	+4.8	+0.7	−14.9 Jan	+3.1 Jan	+4.0	+4.2	10.5 Jan‡‡
Russia	+1.1 Q4	na	+6.0	+1.0	−16.0 Jan	+13.4 Jan	+12.6	+14.1	8.1 Jan‡‡
Sweden	nil Q3	−0.4	+0.6	−1.0	−20.3 Dec	+1.3 Jan	+3.2	+3.4	7.3 Jan‡‡
Switzerland	+1.7 Q3	+0.1	+1.8	−1.0	+0.7 Q3	+0.1 Jan	+2.4	+2.3	2.9 Jan
Turkey	+0.5 Q3	na	+1.5	−1.5	−17.6 Dec	+9.5 Jan	+8.2	+10.4	12.3 Q4‡‡
Australia	+1.9 Q3	+0.3	+2.2	+0.3	+3.8 Q3	+3.7 Q4	+3.0	+4.4	4.8 Jan
Hong Kong	−2.5 Q4	−7.8	+3.1	−4.7	−6.7 Q3	+3.1 Jan	+3.3	+4.3	4.6 Jan††
India	+7.6 Q3	na	+5.3	+5.0	−2.0 Dec	+9.7 Dec	+5.5	+8.2	6.8 2008
Indonesia	+5.2 Q4	na	+6.1	+1.9	−2.8 Dec	+9.2 Jan	+5.6	+10.3	8.4 Aug
Malaysia	+4.7 Q3	na	+5.1	−0.3	−15.6 Dec	+3.9 Jan	+2.3	+5.5	3.1 Q3
Pakistan	+5.8 2008**	na	+6.0	+1.2	−1.2 Nov	+20.5 Jan	+11.9	+20.3	5.6 2007
Singapore	−4.2 Q4	−16.4	+1.2	−7.2	−29.1 Jan	+2.9 Jan	+6.6	+6.5	2.6 Q4
South Korea	−3.4 Q4	−20.8	+2.6	−5.9	−18.6 Dec	+3.7 Jan	+3.9	+4.7	3.3 Jan
Taiwan	−8.4 Q4	na	+1.8	−6.5	−43.1 Jan	+1.6 Jan	+2.9	+3.5	5.3 Jan
Thailand	−4.3 Q4	−22.2	+3.0	−1.8	−18.8 Dec	−0.4 Jan	+4.3	+5.5	1.4 Dec
Argentina	+4.9 Q4	−1.2	+6.0	−2.7	−4.4 Jan	+6.8 Jan	+8.2	+8.6	7.3 Q4‡‡
Brazil	+6.8 Q3	+7.4	+5.3	+1.6	−14.5 Dec	+5.8 Jan	+4.6	+5.7	8.2 Jan‡‡
Chile	+4.8 Q3	−0.2	+3.5	+1.0	−3.7 Dec	+6.3 Jan	+7.5	+8.7	7.5 Dec††‡‡
Colombia	+3.1 Q3	+2.9	+2.8	−1.0	−13.3 Nov	+7.2 Jan	+6.0	+7.0	10.8 Nov‡‡
Mexico	−1.6 Q4	−10.3	+1.5	−1.8	−6.7 Dec	+6.3 Jan	+3.7	+5.1	5.0 Jan‡‡
Venezuela	+4.6 Q3	na	+4.9	−3.0	+2.4 Nov	+30.7 Jan	+24.1	+30.4	6.3 Q4‡‡
Egypt	+5.9 Q3	na	+7.2	+4.9	+7.3 Q3	+14.4 Jan	+10.5	+18.3	8.6 Q3‡‡
Israel	+1.2 Q4	−0.5	+4.1	+0.4	+1.2 Dec	+3.3 Jan	+3.5	+4.6	5.9 Q3
Saudi Arabia	+3.5 2007	na	+4.2	+0.4	na	+7.9 Jan	+5.8	+9.4	na
South Africa	+1.0 Q4	−1.8	+3.1	−0.8	−7.0 Dec	+8.1 Jan	+9.3	+11.3	23.2 Sep‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	−9.4 Q4	na	−2.8	−5.0	−20.7 Dec	+4.1 Jan	+11.0	+10.4	8.3 Nov
Finland	+1.3 Q3	+0.4	+1.6	−1.3	−15.6 Dec	+2.2 Jan	+3.9	+4.1	6.6 Jan
Iceland	−0.8 Q3	−5.5	−0.5	−9.7	+0.4 2007	+17.6 Feb	+6.8	+13.8	4.8 Dec‡‡
Ireland	+0.1 Q3	+4.7	−2.8	−4.8	−12.3 Dec	−0.1 Jan	+4.3	+4.1	9.2 Jan
Latvia	−10.5 Q4	na	−4.6	−12.0	−14.2 Dec	+9.8 Jan	+15.8	+15.4	9.0 Nov
Lithuania	−1.5 Q4	−9.3	+3.7	−4.8	na	+9.6 Jan	+9.9	+10.9	7.0 Jan‡‡
Luxembourg	−0.3 Q3	−5.5	+0.6	−2.8	−15.9 Nov	+0.5 Jan	+3.3	+3.4	5.0 Dec‡‡
New Zealand	−1.4 Q3	−2.7	−0.9	−3.2	−0.5 Q3	+3.4 Q4	+3.2	+4.0	4.6 Q4
Peru	+4.9 Dec	na	+9.8	+3.1	+5.1 Nov	+6.5 Jan	+4.2	+5.8	8.1 Dec††
Philippines	+4.5 Q4	+4.1	+4.3	−0.5	−6.6 Nov	+7.1 Jan	+4.9	+9.3	6.8 Q4‡‡
Portugal	−2.1 Q4	−7.8	nil	−2.8	−11.4 Dec	+0.2 Jan	+2.9	+2.6	7.7 Q3‡‡
Slovakia	+2.7 Q4	na	+6.8	+2.0	−16.7 Dec	+3.7 Jan	+3.8	+4.6	9.0 Jan‡‡
Slovenia	+3.8 Q3	na	+4.0	+0.5	−17.5 Dec	+1.6 Jan	+6.4	+5.7	7.0 Dec‡‡

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions.- §RPI inflation rate 0.1% in Jan. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. ***Centred 3-month average

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

The Economist commodity-price index

Feb 26th 2009
From The Economist print edition

The Economist commodity-price index

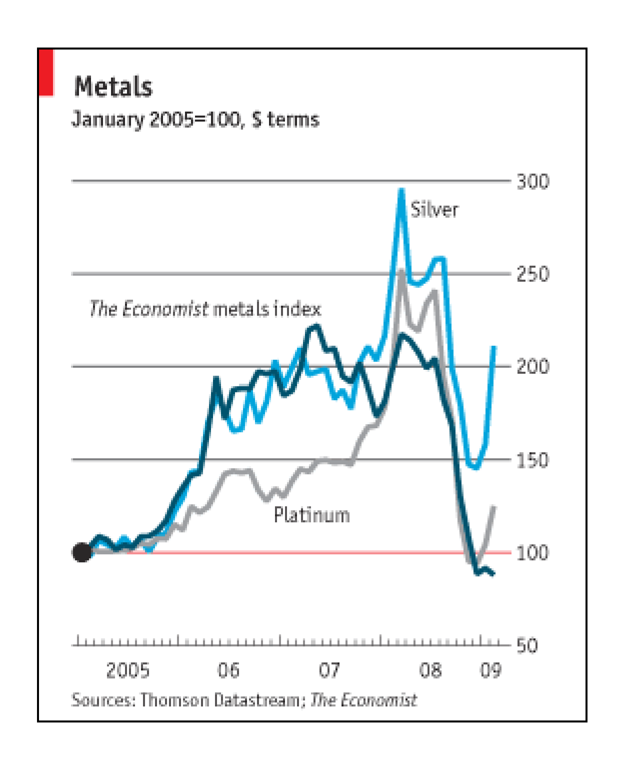
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	Feb 17th	Feb 24th*	% change on one month	% change on one year
Dollar index				
All items	155.2	150.6	-6.6	-41.7
Food	183.9	178.9	-6.5	-30.4
Industrials				
All	118.1	114.0	-6.6	-56.1
Nfa†	110.7	107.5	-7.5	-45.5
Metals	122.2	117.6	-6.2	-60.0
Sterling index				
All items	165.1	158.4	-8.2	-20.3
Euro index				
All items	114.2	109.2	-3.5	-31.9
Gold				
$ per oz	969.80	974.25	+8.2	+3.3
West Texas Intermediate				
$ per barrel	34.96	39.97	-4.9	-60.4

*Provisional †Non-food agriculturals.

Metals

Feb 26th 2009
From The Economist print edition



Metal prices have fallen sharply in the past year, as manufacturing industry has sunk into deep recession. Base metals have lost the most ground, falling by 60% since their peak in March last year. Some precious metals have suffered too: silver and platinum prices fell by more than half from their peaks before bottoming out at the end of last year. But they have enjoyed a revival in 2009, as pessimistic investors have sought havens for their savings. The gold price has captured the headlines, flirting with the $1,000 barrier that it temporarily breached last March. But silver prices have risen twice as quickly as gold prices since the start of the year. Platinum prices have also benefited from the rush to safety.



Trade, exchange rates, budget balances and interest rates

Feb 26th 2009
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2008†	Currency units, per $ Feb 25th	Currency units, per $ year ago	Budget balance % of GDP 2008†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−820.6 Dec	−697.9 Q3	−4.6	–	–	−3.2	0.51	2.92
Japan	+38.5 Dec	+156.0 Dec	+3.6	97.0	107	−3.1	0.60	1.31
China	+314.8 Jan	+371.8 2007	+10.2	6.84	7.14	−0.1	1.28	3.03
Britain	−173.0 Dec	−45.6 Q3	−2.2	0.70	0.50	−5.3	2.10	3.45
Canada	+45.8 Dec	+19.2 Q3	+1.0	1.26	0.98	0.3	0.65	3.31
Euro area	−46.4 Dec	−88.9 Nov	−0.4	0.79	0.66	−1.7	1.85	2.99
Austria	−1.5 Nov	+16.8 Q3	+3.1	0.79	0.66	−0.6	1.85	4.16
Belgium	+5.6 Nov	−8.2 Sep	+0.4	0.79	0.66	−0.9	1.87	4.10
France	−79.6 Dec	−56.1 Dec	−1.8	0.79	0.66	−3.2	1.85	3.57
Germany	+264.5 Dec	+237.0 Dec	+6.6	0.79	0.66	0.2	1.85	2.99
Greece	−67.0 Nov	−51.2 Dec	−13.3	0.79	0.66	−3.9	1.85	5.43
Italy	−16.6 Dec	−72.4 Nov	−2.8	0.79	0.66	−2.9	1.85	4.53
Netherlands	+52.7 Dec	+67.6 Q3	+6.9	0.79	0.66	1.0	1.85	3.65
Spain	−139.3 Dec	−159.1 Nov	−9.8	0.79	0.66	−3.6	1.85	3.94
Czech Republic	+4.4 Dec	−6.6 Dec	−3.1	22.4	16.6	−1.5	2.49	4.87
Denmark	+5.6 Dec	+6.0 Dec	+1.0	5.87	4.94	3.3	3.81	3.65
Hungary	nil Dec	−11.3 Q3	−5.5	237	171	−3.4	9.51	11.71
Norway	+76.3 Jan	+86.5 Q3	+18.3	6.90	5.20	19.8	3.21	3.86
Poland	−23.7 Dec	−28.5 Dec	−5.7	3.70	2.34	−1.9	4.60	5.95
Russia	+179.8 Dec	+98.9 Q4	+6.0	35.8	24.1	5.5	13.00	11.20
Sweden	+15.7 Jan	+40.5 Q3	+7.3	8.96	6.18	2.6	1.00	2.72
Switzerland	+19.2 Jan	+40.3 Q3	+8.9	1.17	1.07	0.9	0.50	2.02
Turkey	−69.8 Dec	−41.4 Dec	−5.4	1.70	1.18	−1.8	12.90	8.36[‡]
Australia	−4.0 Dec	−56.7 Q3	−5.0	1.55	1.07	−1.9	3.16	4.27
Hong Kong	−26.0 Dec	+26.4 Q3	+9.2	7.75	7.79	−2.1	0.79	1.71
India	−114.5 Dec	−28.5 Q3	−3.6	49.9	39.8	−6.0	4.74	7.09
Indonesia	+8.7 Dec	+3.9 Q3	+0.4	11,945	9,053	−1.2	9.88	11.07[‡]
Malaysia	+42.7 Dec	+38.3 Q3	+11.4	3.67	3.20	−5.1	2.09	4.08[‡]
Pakistan	−20.9 Jan	−15.6 Q3	−6.0	79.9	62.5	−6.8	13.61	23.26[‡]
Singapore	+16.1 Jan	+29.2 Q3	+13.5	1.53	1.40	0.8	0.58	1.84
South Korea	−12.6 Jan	−6.4 Dec	−0.7	1,516	941	0.3	2.52	5.08
Taiwan	+6.2 Jan	+25.0 Q4	+4.1	34.7	30.9	−1.7	0.90	1.47
Thailand	+0.2 Dec	−0.2 Dec	−0.1	35.8	32.1	−0.6	2.05	2.88
Argentina	+12.8 Jan	+9.0 Q3	+2.8	3.55	3.16	1.3	14.56	na
Brazil	+23.3 Jan	−27.0 Jan	−1.9	2.38	1.67	−0.7	12.66	6.16[‡]
Chile	+8.5 Jan	−1.6 Q3	−2.3	603	462	4.5	5.40	3.89[‡]
Colombia	+2.0 Dec	−5.3 Q3	−2.8	2,580	1,854	−0.8	9.02	7.15[‡]
Mexico	−16.6 Jan	−2.4 Q4	−1.9	14.9	10.7	−0.1	7.24	8.43
Venezuela	+50.2 Q3	+49.4 Q3	+14.8	5.65	5.00[§]	−1.1	17.02	6.55[‡]
Egypt	−25.2 Q3	+0.1 Q3	−0.9	5.61	5.50	−6.8	10.51	4.70[‡]
Israel	−13.1 Jan	+2.6 Q3	+1.2	4.20	3.61	−2.1	0.61	3.49
Saudi Arabia	+150.8 2007	+95.0 2007	+26.2	3.75	3.75	33.6	1.15	na
South Africa	−10.9 Dec	−23.2 Q3	−7.6	9.99	7.43	−1.0	9.73	8.27
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−3.6 Dec	−2.2 Dec	−9.6	12.3	10.4	−2.3	6.73	na
Finland	+10.1 Dec	+6.7 Dec	+3.5	0.79	0.66	4.6	1.82	3.76
Iceland	−0.2 Jan	−5.4 Q3	−17.3	113	65.3	0.3	18.13	na
Ireland	+41.4 Nov	−16.4 Q3	−3.3	0.79	0.66	−6.6	1.85	5.40
Latvia	−6.4 Dec	−4.5 Dec	−14.3	0.56	0.46	−2.7	9.70	na
Lithuania	−7.4 Dec	−6.3 Dec	−12.6	2.72	2.29	−1.0	7.03	na
Luxembourg	−7.8 Nov	+4.0 Q3	na	0.79	0.66	−0.1	1.85	na
New Zealand	−3.6 Jan	−11.6 Q3	−8.1	1.96	1.22	−1.0	3.65	4.49
Peru	+3.2 Dec	−3.0 Q3	−3.6	3.25	2.89	2.2	6.35	na
Philippines	−7.6 Dec	+2.9 Sep	+1.8	48.1	40.3	−0.8	5.31	na
Portugal	−34.4 Nov	−29.3 Dec	−10.9	0.79	0.66	−2.4	1.85	4.44
Slovakia	−0.9 Dec	−6.2 Nov	−6.1	23.7	21.7	−2.3	1.35	3.75
Slovenia	−4.7 Dec	−3.1 Nov	−6.1	0.79	0.66	−0.6	1.85	na

*Merchandise trade only. †*The Economist* poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.
Sources: National statistics offices and central banks; Thomson Datastream; Reuters; JPMorgan; Bank Leumi le-Israel; Centre for Monitoring Indian Economy; Danske Bank; Hong Kong Monetary Authority; Standard Bank Group; UBS; Westpac.



Markets

Feb 26th 2009
From The Economist print edition

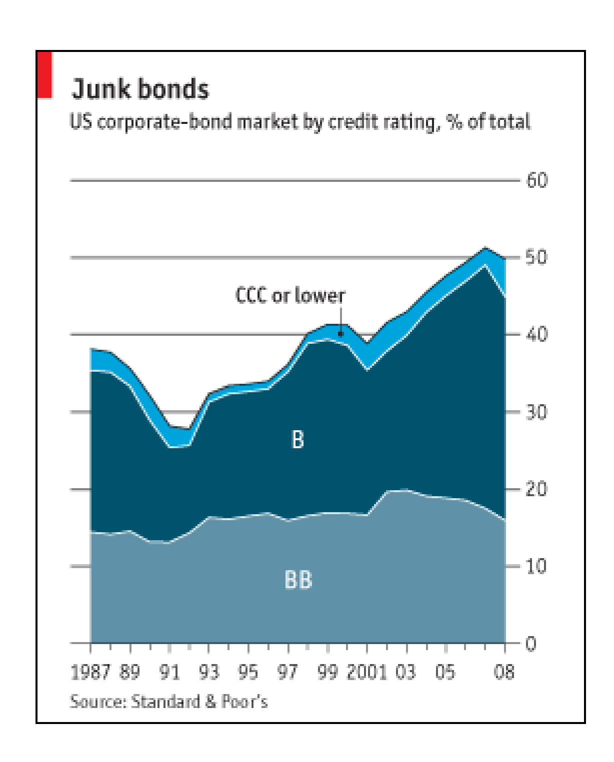
Markets

		% change on		
			Dec 31st 2007	
	Index Feb 25th	one week	in local currency	in $ terms
United States (DJIA)	7,270.9	-3.8	-45.2	-45.2
United States (S&P 500)	764.9	-3.0	-47.9	-47.9
United States (NAScomp)	1,425.4	-2.9	-46.3	-46.3
Japan (Nikkei 225)	7,461.2	-1.0	-51.3	-43.9
Japan (Topix)	745.6	-0.5	-49.5	-41.8
China (SSEA)	2,316.1	-0.2	-58.1	-55.2
China (SSEB, $ terms)	145.6	+5.6	-62.8	-60.2
Britain (FTSE 100)	3,849.0	-3.9	-40.4	-57.4
Canada (S&P TSX)	7,932.3	-3.0	-42.7	-55.1
Euro area (FTSE Euro 100)	605.0	-6.9	-56.0	-61.8
Euro area (DJ STOXX 50)	1,965.3	-7.2	-55.3	-61.2
Austria (ATX)	1,450.9	-2.1	-67.9	-72.1
Belgium (Bel 20)	1,681.1	-4.3	-59.3	-64.6
France (CAC 40)	2,696.9	-6.2	-52.0	-58.3
Germany (DAX)*	3,846.2	-8.5	-52.3	-58.6
Greece (Athex Comp)	1,521.5	-4.3	-70.6	-74.5
Italy (S&P/MIB)	15,218.0	-8.2	-60.5	-65.7
Netherlands (AEX)	220.7	-7.4	-57.2	-62.8
Spain (Madrid SE)	791.6	-4.8	-51.8	-58.1
Czech Republic (PX)	642.1	+2.2	-64.6	-71.2
Denmark (OMXCB)	220.2	-6.0	-50.9	-57.4
Hungary (BUX)	9,886.9	-4.5	-62.3	-72.5
Norway (OSEAX)	254.1	-4.6	-55.4	-64.9
Poland (WIG)	21,422.9	+0.5	-61.5	-74.4
Russia (RTS, $ terms)	538.1	+2.6	-65.7	-76.5
Sweden (Aff.Gen)	185.3	-5.3	-45.6	-60.7
Switzerland (SMI)	4,702.5	-5.1	-44.6	-46.3
Turkey (ISE)	24,152.3	+1.3	-56.5	-70.0
Australia (All Ord.)	3,281.5	-2.5	-48.9	-62.2
Hong Kong (Hang Seng)	13,005.1	-0.1	-53.2	-53.0
India (BSE)	8,902.6	-1.2	-56.1	-65.4
Indonesia (JSX)	1,300.1	-2.3	-52.7	-62.8
Malaysia (KLSE)	896.5	+0.1	-38.0	-44.1
Pakistan (KSE)	5,580.8	-5.1	-60.4	-69.4
Singapore (STI)	1,616.8	-2.1	-53.3	-56.1
South Korea (KOSPI)	1,067.1	-4.1	-43.8	-65.3
Taiwan (TWI)	4,493.7	-0.1	-47.2	-50.7
Thailand (SET)	434.2	-1.2	-49.4	-52.4
Argentina (MERV)	1,019.1	-3.4	-52.6	-58.0
Brazil (BVSP)	38,231.0	-3.6	-40.2	-55.3
Chile (IGPA)	12,143.2	-2.2	-13.7	-28.8
Colombia (IGBC)	7,619.6	-1.7	-28.7	-44.3
Mexico (IPC)	18,200.7	-2.9	-38.4	-55.0
Venezuela (IBC)	37,954.4	+0.2	+0.1	-55.5
Egypt (Case 30)	3,562.3	+0.9	-66.0	-66.5
Israel (TA-100)	597.2	-5.2	-48.3	-52.6
Saudi Arabia (Tadawul)	4,542.1	-4.9	-58.9	-58.9
South Africa (JSE AS)	18,817.6	-5.7	-35.0	-55.5
Europe (FTSEurofirst 300)	716.2	-6.2	-52.5	-58.7
World, dev'd (MSCI)	763.8	-3.5	-51.9	-51.9
Emerging markets (MSCI)	505.4	-2.1	-59.4	-59.4
World, all (MSCI)	190.3	-3.3	-52.8	-52.8
World bonds (Citigroup)	756.3	-0.9	+3.5	+3.5
EMBI+ (JPMorgan)	388.0	+0.9	-10.5	-10.5
Hedge funds (HFRX)‡	1,030.1	-0.6	-22.5	-22.5
Volatility, US (VIX)	44.7	48.5	22.5	(levels)
CDSs, Eur (iTRAXX)†	179.0	+4.6	+253.7	+207.1
CDSs, N Am (CDX)†	241.3	+2.6	+209.8	+209.8
Carbon trading (EU ETS) €	9.7	+0.3	-57.4	-63.0

*Total return index. †Credit-default swap spreads, basis points.
Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac. ‡Feb 24th

Junk bonds

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Just under half of corporate debt in America was rated as "speculative" (BB or below) at the end of last year, according to Standard & Poor's, a rating agency. The share of junk-bond issuers in the corporate-bond market had risen from a low of 28% in 1992. Most of the increase in junk issuance was in the B category. The increase reflects the expansion of capital markets to embrace more marginal firms. But it also owes something to the fashion for more leveraged balance sheets, since the quality of corporate debt has fallen at the top of the scale too. Almost all of the increase in investment-grade corporate issues since 1992 has been rated BBB. The share of corporate bonds graded A or higher has declined sharply since then.